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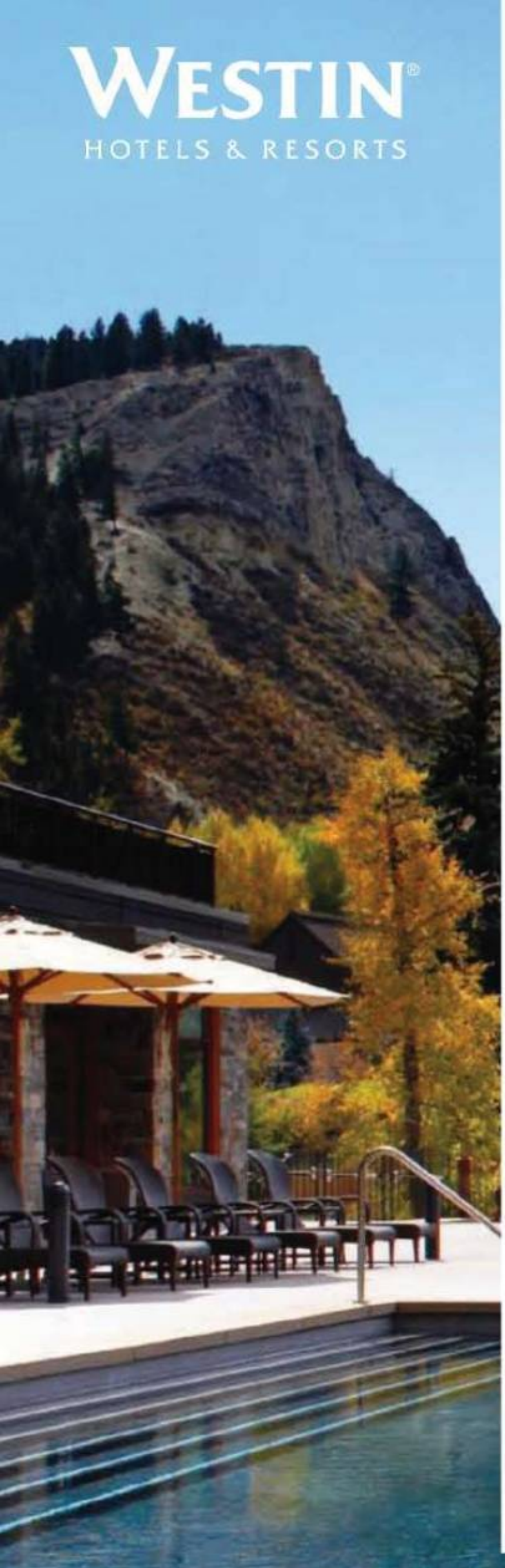
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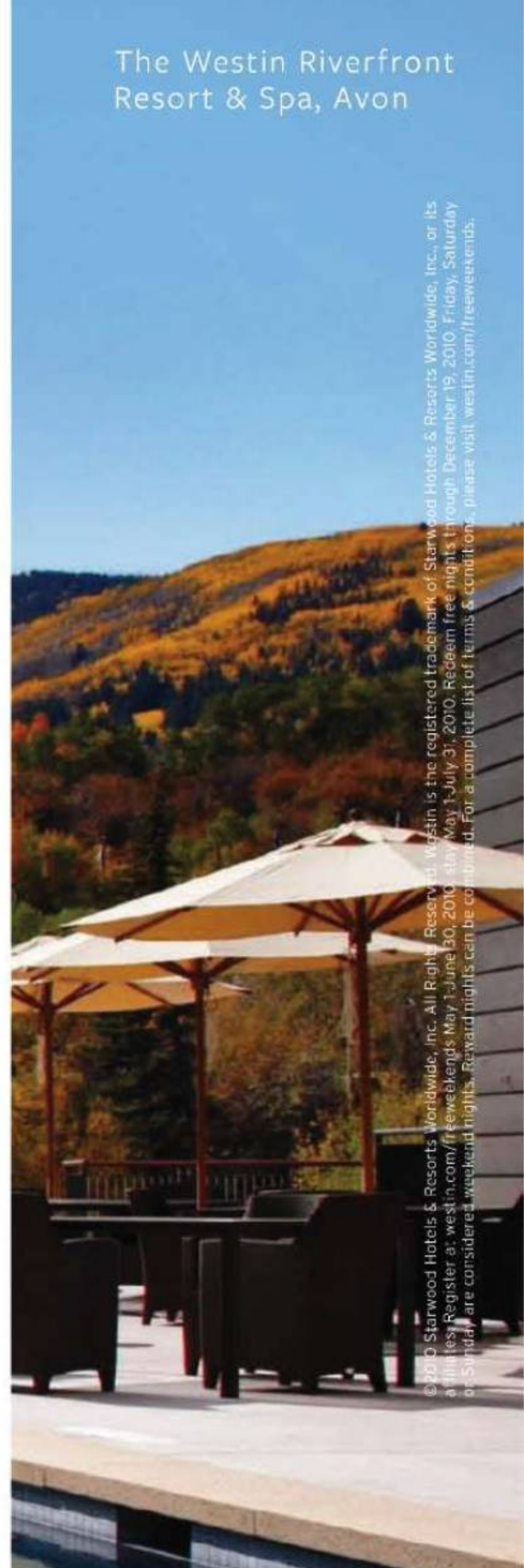
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Corrections & Clarifications

❸ "Subprime Lending Returns to the U.K." (Markets & Finance, May 31) said "GE Money is lending to people who have defaulted on loans, including mortgages, twice before..." GE Money does not grant mortgages to people who have defaulted on mortgages.

How to Reach Us

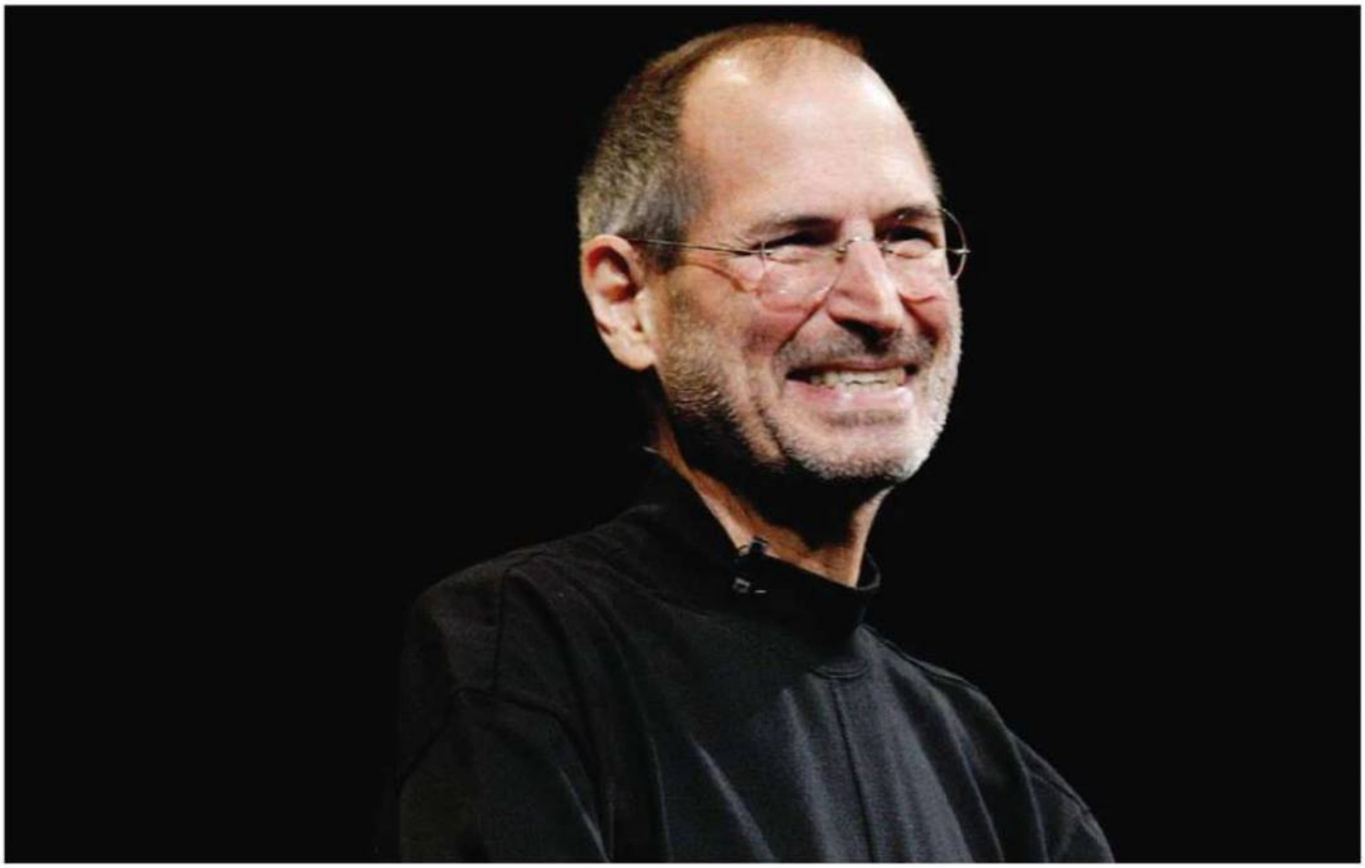
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Opening Remarks



The Last Pitchman

Despite leaks and glitches, Steve Jobs proves once more that when it comes to chanelling desire, no one else comes close.
By Devin Leonard

America has three indigenous art forms: jazz, baseball, and outrageously effective marketing stunts. The self-proclaimed father of public relations, Edward Bernays, was Austrian by birth (he was Sigmund Freud's nephew), but his genius blossomed in New York City in 1929 when he made smoking fashionable for women by marching models down Fifth Avenue waving their "torches of liberty."

America's reigning monarch of marketing is of course Steve Jobs, the Apple chief executive officer who has lately been taking a page from Bernays by describing the iPad as a weapon of freedom–"freedom from programs that steal your private data," as he wrote in a May e-mail exchange with a tech writer. "Freedom from programs that trash your battery. Freedom from porn."

Jobs may be the last true descendant of Bernays, the last great pitchman capable of making vasts swaths of the fractured American public take notice of his latest wares all at the same time. He is famous for his obsessions, such as keeping new products under wraps until he can roll them out at glitzy, tightly scripted, massively observed events. In April, however, a junior Apple engineer left a prototype of the then-unreleased iPhone 4 in a Redwood City (Calif.) bar. Gizmodo, a popular tech blog, got its hands on the device and broke the news about its impressive new features–its uncanny thinness, its high-res display, its forward-facing camera designed to let users video chat with their friends. Nothing was left for Jobs to reveal.

Jobs may be the only one still capable of making vast swaths of the fractured public want the same thing

So how is it that when he unveiled the phone on June 7 at the Moscone Center in San Francisco, the event still had the aura of magic? Jobs tossed off the perfect quip about the Gizmodo incident–"Stop me if you've seen this before"–then demonstrated what he called "the most precise, beautiful thing we've ever designed." Wi-Fi went down during his presentation–and it didn't matter. Like all great salesmen, Jobs knows that controlling the product is a lot less important than controlling our desire.

Jobs didn't create the modern product launch. Hollywood, which

PAUL SAKUMA/AP PHOTO

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is in the business of building and marketing an endless stream of new products, discovered long ago that audiences may be fickle, but their appetites can be stoked. (Even Russell Crowe is easier to control than word of mouth.) So movie studios orchestrate dramatic buildups–trailers, posters, puffball TV, Web teasers–that crescendo at glittering premieres where the stars come out, creating additional entertainment value. For hardcore movie fans, what happens before the movie hits theaters can be as enthralling as the film itself.

The car industry understands the rollout as well. It introduces new products at trade shows that have morphed over the years from dealer gatherings to highly produced events targeted at consumers. Car buffs show up with their friends and spend the day ogling the new chrome and the shapely spokesmodels. "It's like a day at a theme park," says Eric Hirshberg, chief creative officer of ad agency Deutsch's Los Angeles office.

Jobs brought the Hollywood-style rollout to the tech industry in 1984 when he set out to make the launch of the first Mac a pop cultural milestone not unlike the first *Star Wars* movie, which he studied closely. He commissioned the most famous Super Bowl commercial in history, the futuristic "1984" spot directed by Ridley Scott (*Blade Runner*) in which a freedom-loving woman hurled a hammer through a giant computer screen from which a totalitarian figure was lecturing a room full of worker drones. The hammer of liberty was a not-so-subtle metaphor for Apple's struggle against IBM.

Jobs personally demonstrated that first Mac in an auditorium full of cheering fans. In his double-breasted blue blazer and green bow tie (since replaced by a black mock turtleneck), he looked like a character from *Willy Wonka & the Chocolate Factory*. "He wanted to stop the world in its tracks," says Steve Hayden, now vice-chairman of Ogilvy & Mather, who worked on the first Mac campaign.

Shortly thereafter Jobs was fired, and the company floundered for 12 years, losing its mystique as well as its profits. He returned in 1997 and the rollouts–iMac, iPod, iPhone, iPad–have become self-propagating events in which the media ritualistically attempts to ferret out advance details, and Apple keeps the rabbit in the hat. What made the iPhone 4 launch worth watching was its departure from the usual script. Gizmodo created a global stir on Apr. 19 when it posted a picture of the new phone. "We got it," the blog boasted. "We disassembled it. It's the real thing, and here are all the details."

"We sometimes think that in a connected, interactive world, salesmanship is no longer effective. It isn't true."
Kelly O'Keefe, advertising scholar

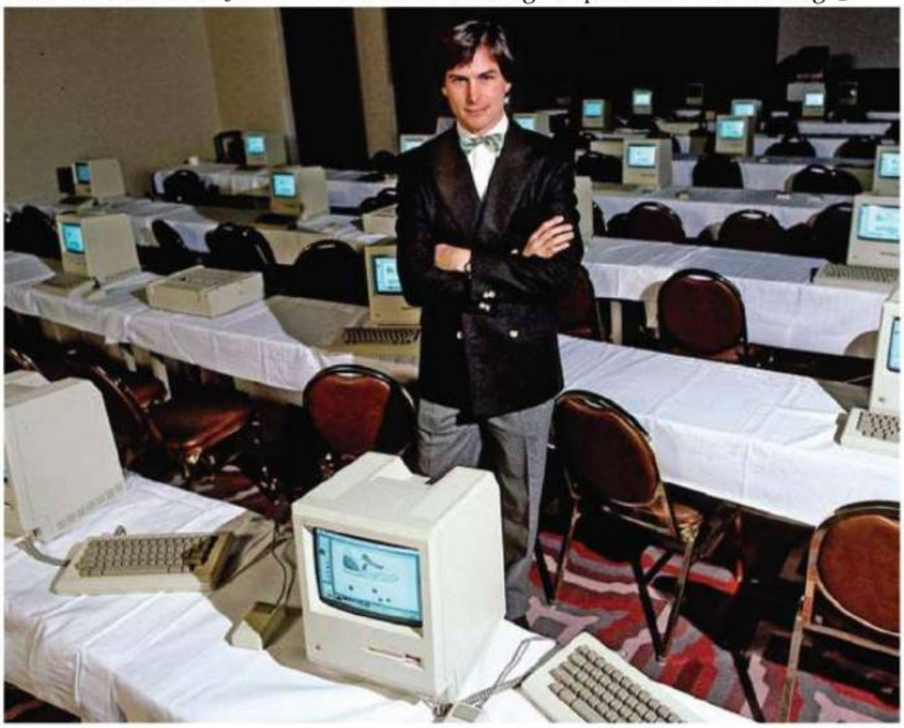
It's a sign of Jobs' mystique that some people wondered whether the iPhone-on-a-barstool snafu might be a piece of diabolically clever guerrilla marketing designed to stir prelaunch buzz. The hapless engineer who left the prototype in the bar "created a ton of chatter out there," says Dean Crutchfield, senior partner at Method, an agency that advises companies about the care and feeding of their brands. "Whether it was intentional or not, my God did it work! He should get a bonus. It also shows that Apple has a drink once in a while." In other words, even when Jobs fumbles a rollout, he still comes out looking smart.

There was something endearing about seeing Jobs struggle with technical difficulties on June 7. It turns out that even the CEO of Apple can't get his phone to work sometimes. We all know how that feels, especially those of us in bandwidth-challenged metropolises who must rely on AT&T's spotty cellular service. Jobs also got a laugh when he insisted that journalists and bloggers turn off their laptops and stop hogging bandwidth. The media complied, as it so often does when Jobs commands.

Jobs makes all of this look easy. Of course, it's not. Hewlett-Packard chose the same day to present its new smartphone-compatible printers. These are products many of us will soon be using, but the HP event was drowned out by Apple's. HP says its rollout was locked in before Apple's was announced. HP CEO Mark Hurd can't help it if Jobs makes the weather.

With the media landscape so fragmented, stopping the world in its tracks isn't easy anymore. "We sometimes think that in a connected, interactive world, salesmanship is no longer effective," adds Kelly O'Keefe, executive director of the Virginia Commonwealth University Brandcenter, an advertising studies program. "But it's not true. We are still attracted to it. We are looking for it. We need something to believe in. People believe in Apple. They believe in Jobs."

He's the last great pitchman. Until the next great pitchman comes along


The impresario-in-training, selling the original Mac in 1984

MICHAEL L. ABRAMSON

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Smarter business for a Smarter Planet:

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Global Economics



Workers outside a Honda plant in Foshan demand higher wages

SAM TSANG/SCMP

A New Labor Movement Is Born in China

▶ **Angry migrant workers use new tools—the Internet and 787 million mobile phones**

▶ **"Every worker is a labor lawyer by himself. They know their rights better than my HR officer"**

A nondescript Beijing suburb was recently the venue for an evening of radical politics. The New Labor Art Troupe, a performance group with a cast of laborers, ran a graphic photo of a **Foxconn** worker who had just killed himself. Poems were read commemorating the hard lives of migrant workers in electronics factories and on construction sites. A guitar and harmonica were hauled out and songs were sung with titles like *Marginalized Life*, *Industrial Zone*, *Working Is Our Glory and Our Hell*, *Get Back Our Wages*, and *Fighting in Solidarity*. Some of the hundred or so assembled migrant workers, many of them employed in small furniture factories around the capital, started crying. The evening ended with the crowd standing up for a Chinese rendition of the *The Internationale*, the old battle hymn of the worldwide socialist movement. "The atmosphere was militant, but there was no overt criticism of the government," says University of Hawaii political scientist Eric Harwit, who attended the two hour-plus evening performance on May 28. "They seemed really sincere that they were upset about migrant labor working conditions."

The recent Beijing performance is just one example of the rising labor activism now evident in China, activism that asserted itself in recent weeks at the factories of Foxconn and **Honda Motor**. It includes groups like New Labor, yet it also encompasses legal aid and other support networks at scores of universities, law firms focused on promoting worker rights, and countless migrant worker aid associations. "Civil society organizations are growing more powerful. They will push China to change," says Li Fan, director of the Beijing-based nongovernmental organization World & China Institute. Li has worked closely with labor groups as well as those pushing grassroots democracy.

More workers understand their rights, and more groups are organizing to support them

The question is whether these groups can spawn a workers' movement that has the organi-

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zation and mass to challenge factory owners across the country. Until a few years ago the Chinese authorities broke up sporadic workers' protests with relative ease: Local officials arrested a few ringleaders, then quickly offered concessions to the rest of the strikers to stop the unrest. Above all else, the Chinese security apparatus made sure that the leaders of labor protests in Shenzhen, Harbin, and elsewhere didn't connect with each other to form a national movement.

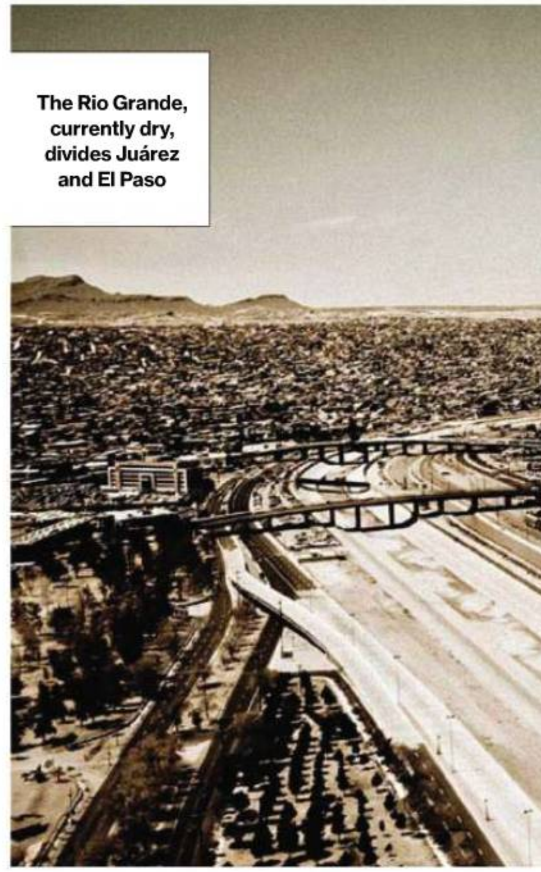
Today's young workers may be harder to corral. China now has 787 million mobile-phone users and 348 million Internet users—and migrant workers in their twenties are far more aware of world developments than their parents. The younger generation can follow labor actions as they unfold, whether in China's northeastern Rust Belt or southern Pearl River Delta. "They have access to information. They use their mobile phones for messaging, to send pictures and video, and to go online," says Chinese Academy of Social Sciences journalism professor Bu Wei, who is researching the use of media by migrant workers.

The more assertive workers have also benefited from a huge push by China's state-run media to popularize knowledge about the tough labor contract law promulgated in 2008. As a result, young workers know what's owed them, whether it be guarantees of double pay for overtime or safer working conditions. "Every worker is a labor lawyer by himself. They know their rights better than my HR officer," says Frank Jaeger, a German factory owner who produces cable connectors in Dongguan in Guangdong Province. Adds Harley Seyedin, president of the American Chamber of Commerce of South China: "There are Internet cafés everywhere, so the workers can get information. They are starting to ask for more. The days of cheap labor are gone."

The workers' ranks are now filled with self-starters like Xu Haitao. A 28-year-old technician in a small metal components factory in Shenzhen, Xu takes a class on labor law and worker rights every Sunday at a local migrant workers support center. "Of course, more and more workers understand their rights these days," says Xu, who surfs labor law sites regularly. "Last year I started using my own computer. Computers are not expensive anymore. I bought the pieces and constructed my own." Xu wants more workers to educate themselves. "Many capitalists and factory managers still abuse our rights," he says. "If all the workers knew the labor law—all 600 million of us—then many factory owners would go bankrupt."

These self-educated workers now have new allies in China's universities. A decade-long effort by Beijing to expand the number of students in China's universities has brought more and more of the rural population—and those with relatives and friends who still work in the factories—onto Chinese campuses. That has driven a wave of support at colleges for migrant workers, points out CASS professor Bu. Students studying law, political science, and social science are forming support groups and even provide legal aid for workers, to a degree not seen before. One of Bu's graduate students, for example, has a brother working for the Foxconn facility near Shanghai.

Many faculty members support their students' activism. "From the Foxconn tragedy, we hear screams coming from the lives of a new generation of migrant workers, warning the entire society to rethink this development model leveraged upon the sacrifice of people's basic dignity," warned an open letter dated May 19 and signed by nine sociologists from prominent schools, including Peking and Tsinghua Universities. "We call for national and local governments to implement practical measures that allow migrant workers to integrate and establish roots in the city ... sharing the fruits of economic development they themselves created."



The Rio Grande, currently dry, divides Juárez and El Paso

ANDREW HARRER/BLOOMBERG

It may be a long summer for Chinese officials trying to contain this unrest. On June 3 more than 20 women workers were detained when police tried to shut down a two-week strike at a formerly state-owned cotton mill in Pingdingshan, Henan. Thousands of workers had stopped operating the looms to express their anger at their factory's privatization and to demand higher wages, reports the Hong Kong-based *China Labour Bulletin*. Although workers are back on the line at the Honda transmission plant that strikers had shut down, their language is anything but conciliatory. "We call all workers to maintain a high degree of unity and not to allow the capitalists to divide us," the Honda workers declared in a statement released on June 3. "We are not simply struggling for the rights of 1,800 workers, but for the rights of workers across the whole country." On June 7, another Honda plant in China went on strike. —*Dexter Roberts*

The bottom line *A new, savvier, and more militant generation of workers may start to form a genuine labor movement in China.*

Quoted

"We are not going to generate a lot of jobs. The cost of labor is too high. We are having a huge substitution of technology for people to save money and make profits."
— Allen Sinai, president, Decision Economics, and former chief economist for Lehman Brothers, speaking about the U.S. economy



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Investment

Bloodied, Juárez Still Lures Big Companies

▶ Despite gang violence, investors are attracted to the Mexican city

▶ "They don't bother us. We don't bother them"

Mexico's Ciudad Juárez is one of the most violent places on earth. Drug gangs fight endless battles with each other and police in the streets and alleys of Juárez' poorest neighborhoods. In the past 28 months this city of 1.5 million, across the Rio Grande from El Paso, has recorded 5,200 murders.

Even though Juárez is the center of Mexico's war on drug dealers, it's holding its own as the center of maquiladoras, the special zones Mexico developed 30 years ago to attract investment. "It's a dual reality," explains Bob Cook, president of the El Paso Regional Economic Development Corp., a group that encourages multinationals to invest on both sides of the border.

In return for building factories in the maquiladoras, multinationals get favorable tax treatment, pay low wages (sometimes as low as $4.21 a day), and take advantage of worker training sponsored by the local government. After mass layoffs during the recession, Juárez factories have added 27,000 workers in the past 10 months. Blue chips like **Johnson & Johnson**, **Delphi Automotive**, and **Scientific Atlanta** show no signs of leaving. *El Diario*, the local daily, is filled with help-wanted ads from **Lear**, **Delphi**, **Siemens,** and other companies. Through April, nine companies had obtained permits to operate in Juárez, about the same as last year. K. Alan Russell, who runs industrial parks in Juárez for dozens of corporate clients, mostly American, says he has landed more business in 2010 than all of last year.

Proximity to the U.S. is a big reason for Juárez' staying power as a place to invest, though drug gangs like their proximity to their American customers, too. Companies have direct access to the U.S. market, and freight trucks can go easily from a Juárez factory to U.S. Interstate 10. "From taking the

➜

Global Fiscal Policy

Deficit Busting

Government budget cutters have the sharp knives out. Below, some examples.
— *Caroline Winter*

U.S.

A budget proposal includes a three-year freeze on nonsecurity discretionary funding, forces the financial industry to pay back TARP costs, and lets the 2001-03 tax cuts for households earning more than $250,000 expire. It closes loopholes for corporate and upper-income taxpayers.

Britain



To shed half of its $226 billion deficit in five years, the government is seeking backing for the deepest cuts since Margaret Thatcher was Prime Minister. The budget will focus on reducing welfare benefits and public-sector pay.

Germany

Chancellor Angela Merkel wants to reduce the budget by $98 billion by 2014. That means reducing subsidies for families, imposing a tax on air travel, slashing public-sector jobs, and restructuring military procurement. A plan for a replica of a Prussian palace in Berlin is on hold.

Spain

It's cutting public employees' wages 5 percent and plans to freeze pay in 2011. To reduce 20 percent unemployment, it will ease rigid work rules that discourage hiring. The navy may sell some warships.



Ireland

The coalition government aims to shrink the deficit to 3 percent of GDP by 2013 from 14.3 percent in 2009. It has raised the sales tax, introduced a levy on income, and cut public workers' pay by 13 percent. The government may tax real estate and water usage.

Greece



Greece must lower a deficit of 12.7 percent of GDP to 8.7 percent in 2010. The main value-added tax is rising to 21 percent from 19 percent. Fuel, alcohol, and tobacco taxes are going up for a second time this year. Bonuses for civil servants will shrink.

DATA: GOVERNMENT REPORTS, BLOOMBERG NEWS

CLOCKWISE FROM TOP: EROS HOAGLAND/REDUX; MARTIN CLEAVER/AP; THONY BELIZAIRE/AFP/GETTY IMAGES; IAN DAGNALL/ALAMY

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Global Economics

order to delivery, our Juárez plant can get the job done in three to four weeks," says Derek Johnson, chief executive of a Denver-based maker of store mannequins. "When you throw in ocean shipping, it sometimes takes our China plant 10 weeks to fulfill an order." Johnson's experience reflects recent studies that rank Mexican competitiveness right up with China's, thanks to cheaper freight costs, a relatively skilled workforce, and those low wages.

The violence never ceases, however. Part of Cook's PowerPoint pitch for investing in Juárez includes color-coded maps showing which cartels operate where in Mexico. The restaurant industry has been hurt by the violence: Many in Juárez don't go out at night. "It will take a miracle to solve this," says Cook.

Yet Francisco Uranga, **Foxconn**'s chief business operations officer for Latin America, can only recall one murder of a maquila employee that seemed cartel-related. The gangs, it seems, prey mostly on each other. "They don't bother us. We don't bother them," says Uranga. The maquilas operate in closely guarded areas, often on the city's outskirts and a stone's throw from the big bridges to the U.S. This year, bridge traffic is up sharply. "We follow the cycle of the U.S. economy," says Russell, "not the political instability."
—*Christopher Power*

The bottom line *Low wages and freight costs, tax breaks, and location are all persuading companies to stay in Juárez.*



Budget Battles

Renewing the Economic Fight in Japan

▶ The new prime minister will shift the focus away from social goals

▶ Now the priority is "going to be economic policy"

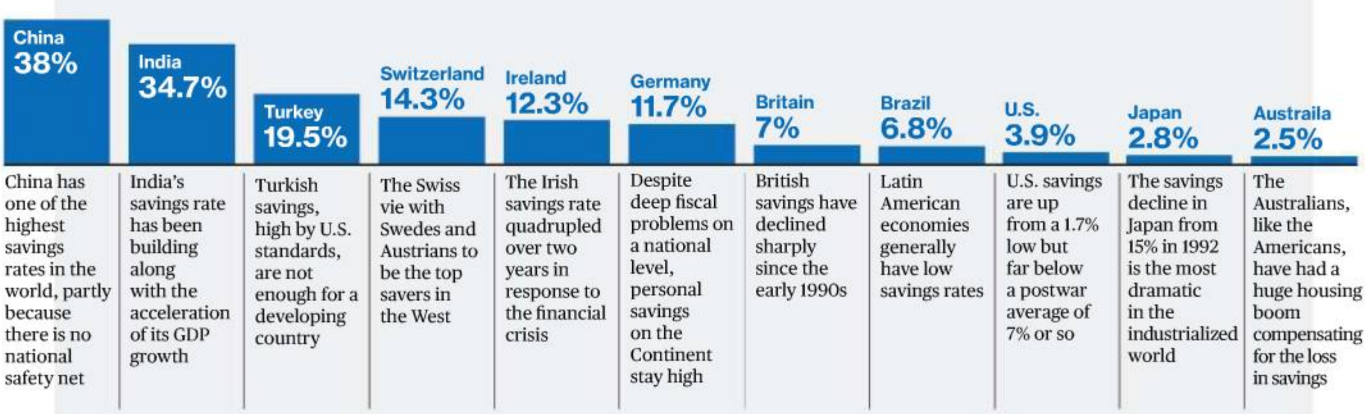
Last year, Yukio Hatoyama was elected Japan's Prime Minister after promising to ease the pain of recession with programs such as better day care and cheaper highway tolls. Naoto Kan, who succeeded him after nine months, is betting a different set of issues will appeal to the beleaguered Japanese. Under Hatoyama, who resigned on June 2, "the No. 1 priority was social policies," says Jesper Koll, head of equity research at JPMorgan Chase in Tokyo. "Now it's going to be economic policy." Adds Eisuke Sakakibara, one of Japan's best-known postwar finance officials: "Kan is a realist."

Kan, the former Finance Minister, takes office as the government prepares to announce by the end of the month its plan for reducing public debt and sustaining growth of 3 percent over the next decade, a pace unseen since 1991. Kan believes the key to growth is ending the deflation that has plagued Japan for much of the past decade. In April he caused a stir by calling for an ambitious inflation target of 2 percent. To reach that goal, Kan would likely need to pump more money into the economy. That's tough, given that Japan's public debt is nearly double the country's gross domestic product, the highest level in the developed world. "I don't think fiscal rehabilitation can be done overnight," Kan said on June 3. "At least I'd like to correct the trend in which the public debt keeps increasing endlessly."

To raise funds, Kan may raise the value-added tax, something Hatoyama had pledged not to do until at least 2014. Economists expect Kan to use some of the money to support industries with high growth potential, such as energy, green technology, and health care. The central bank is already doing its part: The Bank of Japan announced in May that it would offer low-interest loans to banks that agree to support the government's targeted industries. The BOJ is "really taking an active role in where credit is being allocated," says Nikhilesh

Savers and Spenders

How Household Savings Stack Up in Asia, the West, and Latin America



DATA: OECD, WORLD BANK, STANDARD CHARTERED, TURKISH STATE PLANNING OFFICE, BRITISH OFFICE FOR NATIONAL STATISTICS

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Bhattacharyya, an economist with researcher Moody's Analytics. "Essentially they are picking winners."

Kan can't do much to help traditional powerhouses such as the electronics and auto industries. When he started as Finance Minister, Kan made headlines by trying to talk down the yen, which had risen sharply against the dollar, causing pain for **Sony**, **Panasonic**, **Toyota**, and other big exporters. Pursuing a weaker-yen policy now, though, isn't a realistic option, says Hiromichi Shirakawa, chief economist in Tokyo with Credit Suisse. Japan has a current account surplus of 4 percent of GDP. Making it even larger by weakening its currency would antagonize the U.S. "Japan cannot boost exports," Shirakawa says.

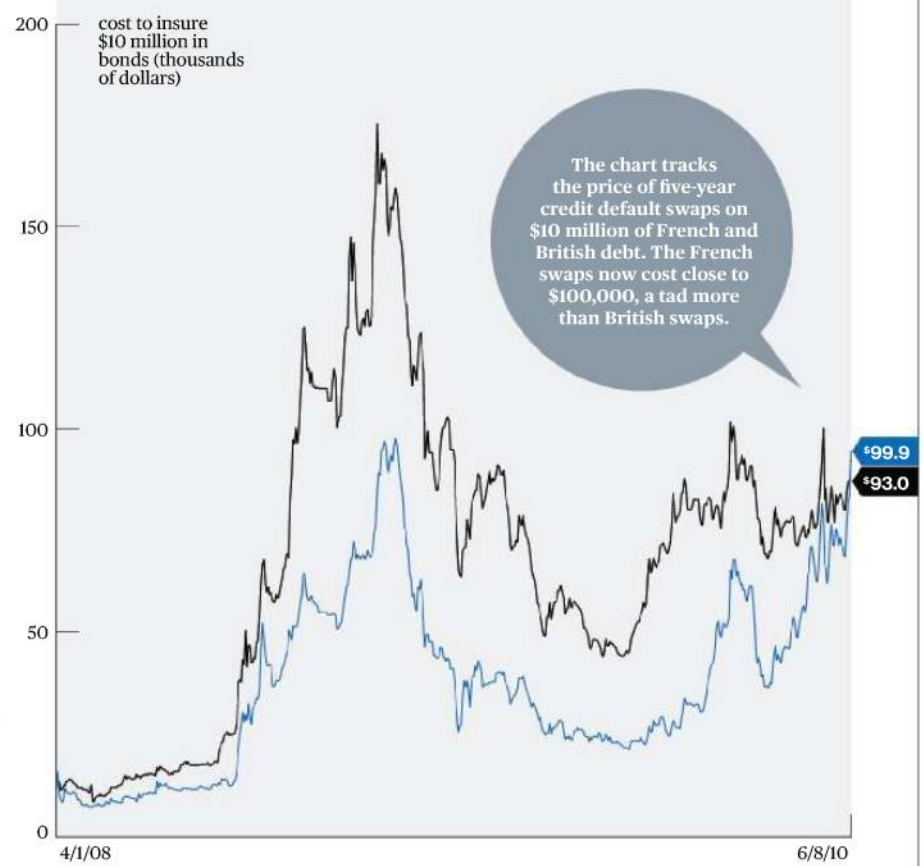
—Bruce Einhorn and Anna Kitanaka

The bottom line *As Naoto Kan takes over as Japan's Prime Minister, he'll likely focus on the economy. The country's huge debt will make his task difficult.*

Sovereign Debt

France Suddenly Looks Risky

While the markets beat up on debt from Greece, Spain, and Portugal this spring, French government bonds were deemed far safer. Of the big European economies, Britain seemed most at risk. Now, for the first time since 2008, the cost of insuring against default on French debt slightly exceeds Britain's. *—John Glover*



Emerging Markets

Growth May Have a Downside for Brazil



OPPOSITE PAGE: HARUYOSHI YAMAGUCHI/BLOOMBERG; THIS PAGE: MARCOS ISSA/BLOOMBERG

- ▶ Shortages hit the economy as GDP races and inflation threatens
- ▶ "Demand is growing at a Chinese pace"

Cia de Bebidas das Américas (AmBev), Latin America's largest brewer, recently had to import beer cans into Brazil for the first time in its 125-year history after local supplies were exhausted. One of Brazil's top sugar producers, **Açúcar Guarani**, left 10 percent of its crop sitting in the fields an extra 40 days because it couldn't acquire enough tires for its harvesters. "We tried to buy directly from China, but they didn't have tires for delivery either," says Jaime Stupiello, agricultural director for Açúcar Guarani. Elsewhere, a truck shortage is pushing up the costs of shipping goods from Brazil's industrial heartland to the rest of the country.

Brazil is experiencing its fastest economic growth in almost two decades, which is what's setting off those nationwide shortages. The country's government statistics office announced on June 8 that gross domestic product expansion hit 9 percent in the first quarter. That's well above the potential growth rate of 4.5 percent most economists have calculated for Brazil. Inflation, now at 5.2 percent, is increasing faster than the government's target of 4.5 percent. Central bank President Henrique Meirelles has jacked interest rates up twice this year, to 10.25 percent. The latest hike was on June 9. He won't stop there, says Elson Teles, chief economist at Maxima Asset Management in Rio de Janeiro. "Demand is growing at a Chinese pace," says Teles. "That's why the central bank will keep raising the Selic [the overnight lending rate]." Meirelles won't explicitly state his policy on interest rates for the rest of the year. He did, however, tell Bloomberg Television on June 4 that the country's economy is "overheating" and policymakers are in a "tightening mood."

It sounds as if the Brazilians are

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about to wage a pitched battle against rampant inflation. Yet here's the puzzle—inflation is higher than the government's target, but it hardly seems out of control. Economists as prominent as New York University professor Nouriel Roubini still think the Brazilian outlook is "very positive," as he told an audience in São Paulo on May 31.

Several issues are at play here. One concerns the economic ghosts that haunt the Brazilians, who endured debilitating bouts of hyperinflation in the recent past. No one wants to see inflation reach gale force. Brazilians are also aware that they can do better at managing the economy. Nearby Peru has lower inflation and still enoys rapid growth.

Meirelles also wants to reassure international bond and stock investors. The former Bank Boston executive did a good job cutting inflation in half from 17 percent in 2003. But many investors feel the central bank kept monetary policy too loose earlier this year after it lowered rates rapidly in 2009 to combat the global recession. Brazilian bond and stock prices suffered, and the currency, which is up 4.4 percent against the dollar overall in the past 12 months, has taken a dive in recent weeks.

Meirelles' tough act is already having an impact. "The market is calmer," says Saddi Castro, chief investment officer at money managers Sul-America Investimentos in São Paulo. Investors are also fully aware that there is a critical national election in October. They want to see the government of President Luiz Inácio Lula da Silva maintain a steady course and avoid the temptation to juice the economy even further to secure votes for the ruling party. Lula is behaving responsibly thus far, and the government is trying to cool things down by cutting government spending.

Finally, Brazil faces an uncertain global economy. There's a risk that double-dip recession in Europe and a slowdown in the U.S. will shrink global demand for Brazil's soybeans, coffee, and iron ore. No one knows for sure. It may be better for Brazil to have its economic house in order in case things get turbulent.

—Carla Simoes and Iuri Dantas

The bottom line *Brazil wants to slow inflation and at the same time keep growing. It's a tough challenge for policymakers.*

Trade

Container Ships: The Stories They Tell

▶ **An index of shipping prices shows demand for goods rising fast**

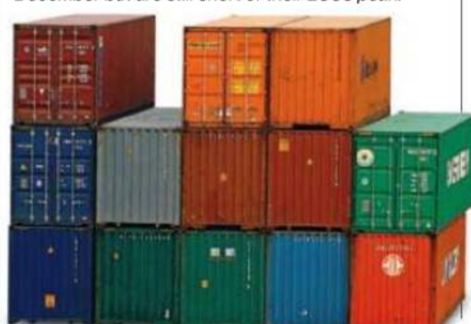
▶ **Some shippers "have seen a remarkable recovery"**

The prices that container ship owners charge for carrying manufactured goods around the world are pretty good indicators of economic activity. Some 90 percent of all trade involves oceangoing ships, so the business of shippers like **Maersk** reflects changes in demand fast. The Hamburg Shipbrokers Assn. of Germany maintains an index that tracks the prices charged by container ship lines. After plunging in 2009 the index has risen every month since, for a total gain of around 97 percent year to date. "They have seen a remarkable recovery," says Harald Serck-Hanssen, global head of shipping, offshore, and logistics at Oslo financial-services group DnB NOR.

While the container index has charged way up, it's still well below its recent peak in the spring of 2008, indicating the global recovery has a long way to go before it recaptures all the ground lost to recession. Philip Damas, a director at Drewry Shipping Consultants in London, figures demand for container ships will cool off in the second half, once stores and factories have replenished inventories, but will remain solid. Separate indexes that track oil tankers and carriers of raw materials like grain have gone up too, though not in the same smooth straight line container ships have followed.

—Meera Bhatia and Alaric Nightingale

The bottom line *Prices charged by owners of container ships have risen around 97 percent since December but are still short of their 2008 peak.*



Tom Keene's EconoChat

Tom talks with **David Rosenberg**, chief economist of Gluskin Sheff & Associates, about double dips and prices

I hate this phrase, but are you predicting a double-dip recession?
I think that what could happen, Tom, is that we have a classic 2002-style growth relapse. There was lots of excitement going into early 2002. We had the inventory contribution. We had all the stimulus coming out of the terrorist tragedies. We built up from a dramatic oversold situation in the stock market. The Nasdaq was up 40 percent from the lows in the opening months of 2002. And look what happened. Real final sales never followed through. And although you didn't have a classic double dip, we had a substantial growth relapse.

Do we have a sustainable real economy now?
If you take a look at some measures like corporate profits, we get a very sharp V-shaped recovery in some sense. But ultimately sustainability is going to come from the demand side. And we are really in uncharted waters here when you review all the postwar data. We are in a secular credit contraction after decades of being in a secular expansion, not just of credit, but also of baby-boomer balance sheets.

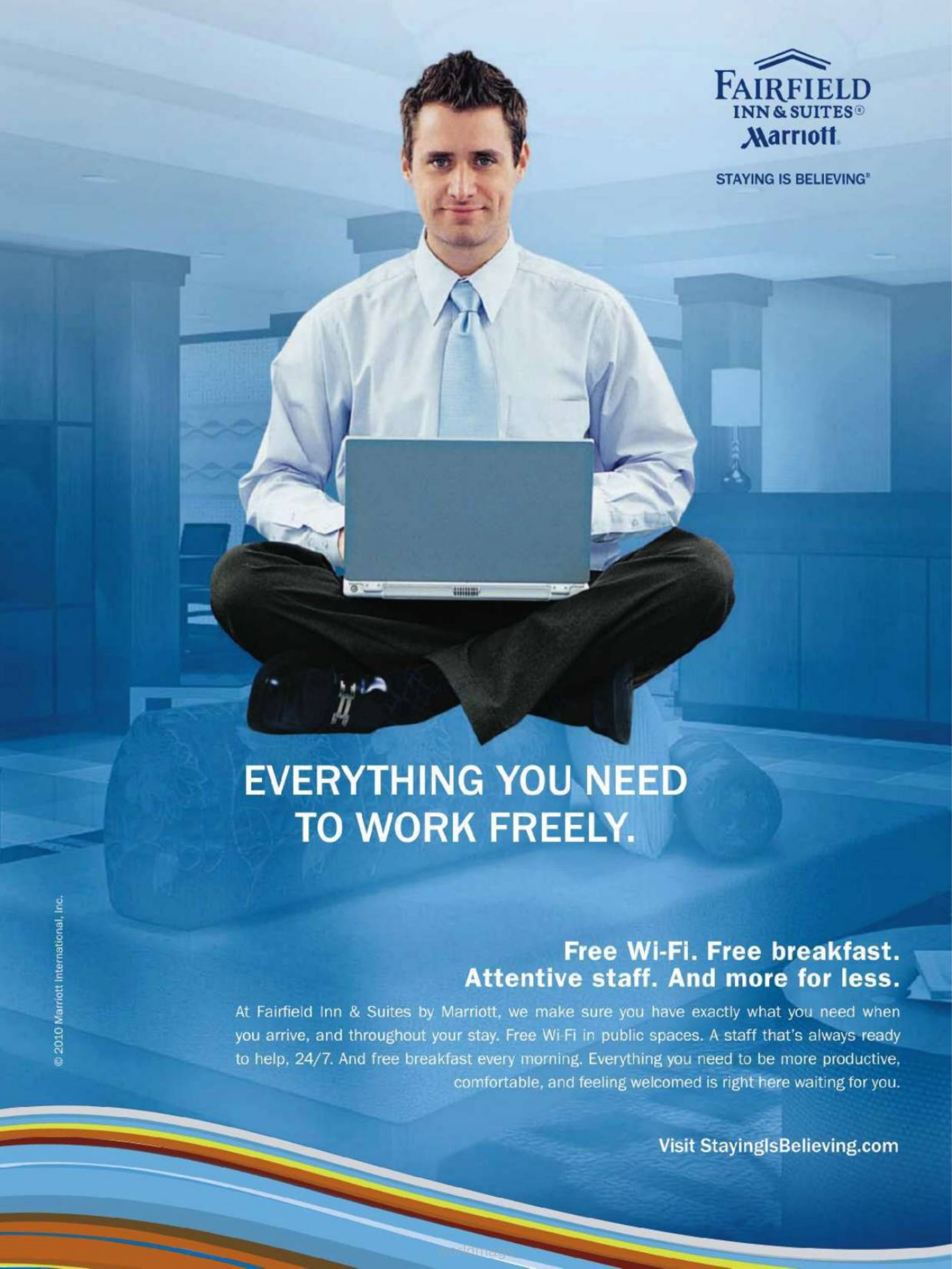
Are we going to see a tempering in commodity inflation?
Well, one of the best interim leading indicators of commodities is the Chinese stock market. It's down almost 30 percent from the peak, and it has got about a three- to six-month lead on the commodity complex. So I do expect that in the next several months commodities will pull back. Ⓑ



Keene hosts Bloomberg Surveillance *7-10 a.m., 1130AM in New York, XM129, Sirius 130.*

FROM LEFT: REUTERS; ANDREW HARRER/BLOOMBERG

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French Women Storm The Corporate Boardroom

▶ A proposed law would require that 40% of corporate board members be female

▶ "I used to be against quotas ... but things are moving too slowly"

A group of women wearing fake beards stormed the podium at **Veolia Environnement**'s crowded shareholders' meeting in Paris last month, challenging Chairman Henri Proglio over the gender makeup of his overwhelmingly male board. "Is it really wise to allow women to define the strategy of a company, a task requiring intelligence, an ability to react, and coolheadedness?" asked a disguised member of the feminist advocacy group La Barbe, or "The Beard." She taunted the French water utility for having only one woman on its 17-member board.

That kind of stunt is becoming common during this season of French annual meetings. The activists, who decline to reveal their identities for fear of retribution, are demanding that companies, including Veolia and insurer **Axa,** deal with the "boy's club" reputation of their corporate suites. Today, management has to take such pranks seriously. French lawmakers are considering legislation that would require at least 40 percent of companies' boards to be made up of women within six years or risk not being able to add new male directors.

The legislation, passed in January by the lower house of Parliament, is being considered by the Senate. If it becomes law, France would join Norway in adopting legally binding quotas to boost the number of female directors. "The quota thing is fine," French Finance Minister Christine Lagarde says in an interview. "I used to be against quotas. You stand on your own merits and you should be recognized as such. But things are moving too slowly. There will be a lot expected of women simply because there will be resentment on the part of those who will have to make space."

Women make up 9.5 percent of 103 French boards tracked by GovernanceMetrics International, a corporate governance research firm in New York. That is far short of the 40 percent that will be required. Among 405 companies in the U.K. tracked by GovernanceMetrics, females account for 8.5 percent. In the U.S., it's 12.2 percent among 1,754 companies studied. In Norway, where the proportion was 6.8 percent when quotas were proposed in 2002, the number is 34 percent among 23 companies.



Chirac, wife of the former President, is now an LVMH director

PASCAL LE SEGRETAIN/GETTY IMAGES

French companies are scrambling to outline plans to raise the percentage of female directors on their boards. Gas utility **GDF Suez** may shrink the size of its board, CEO Gérard Mestrallet told shareholders last month. **Total,** France's largest company, named two men to its board in May but pledged to raise female representation to 18 percent next year by adding a third woman to its 17-member board. **PPR**'s board named three women directors last month, bringing their number to 29 percent. CEO François-Henri Pinault says the luxury goods company will seek to reach gender parity.

The threat of penalties has already brought some unlikely women to French boardrooms: the wives of prominent French men. In recent months, Florence Woerth, wife of Labor Minister Eric Woerth, became a director at luxury goods maker **Hermès**; Nicole Dassault, wife of industrialist Serge Dassault, joined the **Dassault Aviation** board; Amélie Oudéa-Castera, wife of **Société Générale** CEO Frédéric Oudéa took a seat on the board of **Lagardère**; and Brigitte Longuet, wife of French Senator Gerard Longuet, went to **Canal+**.

In April, **LVMH Moët Hennessy Louis Vuitton** CEO Ber-

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nard Arnault surprised shareholders by naming Bernadette Chirac, the 77-year-old-wife of former President Jacques Chirac, to a seat on the LVMH board, after 80-year-old Russian historian Hélène Carrère d'Encausse backed out. In response to a question at a shareholders' meeting, Arnault said the maker of Veuve Clicquot champagne and Fendi purses needed a nominee who brought a "feminine eye" to products and understood countries where LVMH operates. Until Chirac took her seat, Arnault's daughter Delphine was the only woman on LVMH's 17-member board.

"The choice was astonishing," says Viviane Neiter, a corporate governance consultant who queried Arnault at the meeting. "There have been recent nominations at French companies that don't seem altogether helpful." Neiter, who along with Miriam Garnier of the European Professional Women's Network lobbies to get women into boardrooms, says boosting the number of women directors should be used as a way to improve governance in France, rather than trying to meet the quota with unthreatening, politically connected women.

"It would be a huge mistake if boards made quantitative changes to their composition without improving quality," Garnier said. "There is the potential to make cosmetic changes by adding women with political considerations in mind. This would be a terrible distortion of the law."



"Bearded" protesters have demanded more women on French boards

About 170 female directors would have to be found within six years to meet the quota requirement for France's benchmark CAC 40 Index companies and 1,200 for the larger SBF 120 Index, according to Marc G. Lamy, who heads executive search company Boyden France. "This is not mission impossible for headhunters," he said. "There's no dearth of candidates."

Corporate boards have long been criticized for being cozy clubs made up of men from France's elite administrative, business, and engineering schools, known as the *grandes écoles*, who often are CEOs of other big companies. Adding more women to even a fraction of French boardrooms could have a big impact on the nation's highly concentrated power structure. For instance, at CAC 40 companies, where boards are about 12 percent female, 98 directors, or 22 percent of the total, hold 43 percent of the voting rights, according to a study published in October by Ernst & Young and France Proxy, which call the group "the biggest network of influence in French capitalism." —*Tara Patel*

The bottom line *French boardrooms have long been a male domain. A proposal requiring that at least 40 percent of directors be women could change that.*

Energy

Oil-Rich Deep Waters Off Brazil Still Beckon

▶ Despite the Gulf spill, Petrobras continues to drill offshore

▶ "We are using the best practices, the best technology"



State-controlled Petróleo Brasileiro is by far the world's biggest oil producer in waters deeper than 1,000 feet. In 2009, **Petrobras**, which is based in Rio de Janeiro, pumped 20 percent of all oil from deep waters, according to data compiled by PFC Energy, a petroleum industry consultant. Petrobras' closest deepwater rival is **ExxonMobil**, with 13 percent of production.

This deepwater dominance leaves Petrobras more exposed than any oil company on the planet to the risk of an accident similar to the Deepwater Horizon spill in the Gulf of Mexico, the largest in U.S. history. Undeterred, the company is sticking with its aggressive schedule of deepwater drilling; in June alone, Petrobras found a pool of oil estimated to hold 380 million barrels almost three miles below the ocean floor in Brazil's Campos Basin.

Hugo Repsold, an exploration and production manager at Petrobras, says the U.S. moratorium imposed after the Deepwater Horizon spill will not stunt Petrobras' development of offshore fields including Tupi in the South Atlantic deep waters off Brazil, the largest discovery in the Americas since Mexico's Cantarell find in 1976. Petrobras is accelerating investments to more than double oil production by 2020 and thus boost economic growth and employment in Latin America's largest economy. "We are using the best practices, the best technology, the best equipment, and we are confident we can keep drilling all these wells, performing with the necessary safety and environmental care," Repsold says. "The [Brazilian] public, they support these efforts."

Petrobras may even try to hire badly needed drilling rigs at a discount now that the U.S. has curbed deepwater drilling in the Gulf, according to Rebecca Rosen of PFC. "It is very likely that rig contractors will at least try to move rigs out of the Gulf of Mexico," Rosen says. "An overflow of rigs in Brazil would certainly favor Petrobras in its ability to reduce rates." Rosen figures 40 percent of the rigs in the Gulf are able to operate in Brazil. Petrobras declined to comment on plans to hire rigs leaving the Gulf.

Industry analysts and Petrobras' suppliers say the company maintains quality and safety standards that meet and often exceed those of its peers, including **BP**, which operated the oil well whose rupture continues to contaminate the Gulf coast. The U.S. will split up the federal regulator, the Minerals Management Service, following accusations it was too lenient in letting the oil industry monitor offshore drilling itself. In contrast, Brazil's Agência Nacional do Petróleo, or ANP, has long

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3
miles

Depth below the ocean floor of an oil pool found by Petrobras in June off Brazil

kept a much closer eye on operators, says Cleveland M. Jones, a professor of geology at the Universidade do Estado do Rio de Janeiro. "Almost every step of the exploration process up to production is monitored, and reports are sent out regularly about procedures that are undertaken, so there is less self-monitoring here than in the Gulf of Mexico," says Jones, who has done extensive research on Brazil's deepwater oil basins.

Still, Brazil can't escape the risks of drilling wells miles below the ocean floor that penetrate reservoirs where temperatures reach 390F (198C). "[Petrobras] is talking about a large expansion that will substantially increase the possibility, just by probabilities, that accidents could happen," says Christopher Palmer, who oversees $5 billion in emerging market stocks, for Gartmore Investment Management in London.

Petrobras, which started drilling offshore in 1968, has suffered accidents, too. The deadliest was in 1984, when 36 workers died evacuating a burning platform. Eleven workers died in 2001 when a platform exploded and sank into the Atlantic off Rio. Still, Petrobras has little choice but to stay the course: Ninety percent of its proven reserves lie in the deep waters off Brazil.
—*Peter Millard*

The bottom line *The BP catastrophe has prompted a drilling moratorium in the Gulf. Undeterred, Petrobras is aggressively drilling in even deeper water.*

Automobiles

Ford Tries to Jump-Start The Explorer

▶ After a sales plunge, the onetime cash cow gets a risky makeover

▶ "The marketing guys don't want to use the word 'wagon' "

In the late 1990s, at the peak of America's love affair with sport-utility vehicles, North Hills (Calif.) Ford dealer Beau Boeckmann had an entire showroom dedicated to the Ford Explorer. The rugged SUV racked up 300 sales each month for his dealership, and it accounted for most of the profits for **Ford Motor** and its dealers nationwide. These days the gas-guzzling Explorer is a has-been and Boeckmann is lucky to sell five a month. Once the top-selling SUV in America, it today ranks No. 13 among utility models. "The Explorer isn't even on people's radar," he says.

Desperate to revive the brand, Ford this summer will unveil a redesigned 2011 Explorer that goes on sale in the fall for about $30,000. Ford's challenge: Craft a politically correct SUV to win back buyers and beat back critics. That's a lot to ask of the Explorer, an SUV synonymous with the kind of big-rig addiction that nearly destroyed Detroit. "It's a vehicle that has to sell against its name," says consultant Jim Hall of 2953 Analytics in Birmingham, Mich. "People still think of the Explorer as a truck and say, 'I don't want a truck.' "

When Ford began the rehabilitation of the Explorer in 2007, SUVs were quickly falling out of fashion as gas prices surpassed $3 a gallon. Ford was on its way to losing $30 billion from 2006 to 2008, and the Explorer that once generated $10,000 per vehicle in gross profit became a pariah. CEO Alan Mulally, only four months into the job, demanded his staff justify spending about $500 million redesigning a model that seemed to have outlived its usefulness. "Alan told us that we need to convince ourselves that we can truly reinvent the Explorer," recalls product development chief Derrick Kuzak.

Job One was ending the SUV's reputation as a rolling refinery. The current Explorer drinks a gallon of gas every 13 miles in the city and every 19 miles on the highway. That's 27 percent worse than today's SUV leaders like the Honda Pilot and the Chevy Traverse. Ford says poor gas mileage is the No. 1 reason buyers reject the Explorer, which saw sales fall 88 percent over the last decade, from 445,157 in 2000 to 52,190 last year. "We said, 'Oh my goodness, what are we going to do about that?' " says Amy Marentic, an engineer on Explorer who now leads Ford's SUV marketing. "We needed jaw-dropping fuel economy."

To get that, Ford cut Explorer's weight (it won't say how much) by switching the SUV from a heavy pickup truck frame to the same chassis as the Taurus sedan. Designers sculpted the shape to lower wind resistance, further improving fuel economy. Engineers installed the tiniest engine ever in an Explorer—a turbocharged 2-liter, 4-cylinder motor. The result: The Explorer's mileage exceeds the 24 mpg highway rating of its most fuel-efficient rival, the Chevy Traverse. The automaker won't give a specific mpg yet for fear competitors will find a way to top it before the new Explorer goes on sale this fall.

That may solve a practical problem. Yet the thornier issue—perception—remains. "There's the nagging guilt of, 'Am I ruining the planet? What do my neighbors think?' " says marketing manager Craig Patterson.

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So Ford plans to hawk the new fuel-economy numbers in Explorer ads, boasting they're better than some sedans. It probably won't win over "Sierra Club types," Patterson concedes, though it could make buying the new Explorer "guilt-free" for some of the 3.5 million owners of the old model.

The risk for Ford is that, in its quest for fuel efficiency, it may lower the SUV's perceived utility. "When you take an Explorer and put it on a car frame and give it car attributes, well, then you've got a wagon," says Charlie Vogelheim, publisher of automotive researcher IntelliChoice. "But the marketing guys don't want to use the word 'wagon.'"

Then there's the wimp factor. Ford says the towing ability of the new Explorer will be reduced yet will still meet the needs of about 80 percent of current customers. It also will ride lower, limiting its off-road abilities. That could deter some image-conscious SUV buyers. In one focus group, Ford asked eight men how many felt towing was very important to them. Eight hands went up. The same eight men were asked what they tow. They each responded: nothing.

Whether a tamer Explorer appeals to the big-hauling set, Ford can't afford to ignore the growing demand for SUVs with car-like characteristics. That segment has grown to 3.5 million vehicles a year—30 percent of the U.S. auto market. Besides, the truck mania of the '90s isn't coming back. "That," says dealer Boeckmann with a sigh, "was a unique moment in time." *—Keith Naughton*

The bottom line *Ford spent about $500 million to redesign the Explorer. Whether drivers want a tamer, less thirsty version of the SUV remains to be seen.*

Quoted

"I'm convinced GM has sufficient financial resources. The state is not the better entrepreneur."
—Rainer Brüderle, German Economy Minister, on Germany's rejection on June 9 of General Motors' request for $1.3 billion in financial aid for its loss-ridden Opel unit





Zegna in Shanghai: Its boutiques are larger in China than in the West

Apparel

Luxury Clothier Zegna's Marco Polo Moment

▶ The Italian menswear maker is riding the wave of Asian affluence

▶ "If they see it is made in China, they perceive it to be a fake."

The alpine valleys of northern Italy's Piedmont region are dotted with abandoned textile mills, victims of competition from China and other low-cost locales. But at a mountainside factory in the village of Trivero, menswear maker **Ermenegildo Zegna** turns out 2 million meters of sumptuous wool, cashmere, and mohair fabric each year—and China is the biggest buyer.

One-fourth of Zegna's annual sales now go to China. Its off-the-rack suits start at about $1,000. Bespoke garments run from $3,800 to $8,500 in the mainland and have become emblems of China's new wealth. Milan-based Zegna (pronounced Zenya) has more stores in China than either **Louis Vuitton** or **Gucci** and commands as much loyalty from Chinese clients as those larger global brands, says Shaun Rein, managing director of Shanghai's China Market Research Group. Although many of its Chinese customers are middle class, "they view themselves as on the way to total affluence," Rein says, and the Italian suitmaker plays brilliantly to that ambition.

Zegna, a century-old, family-run business with $974 million in sales, is proving that even a smallish player can thrive in the world's hottest luxury market. Bain & Co. estimates that Chinese luxury spending will grow 15 percent this year, to more than $11.3 billion, far outpacing the average 4 percent growth seen for the $187 billion industry worldwide. Zegna now has 60 boutiques on the mainland, including dozens in such smaller regional cities as Taiyuan, in northern China, and Urumqi, near the Gobi Desert, where few luxury brands have ventured.

Chief Executive Officer Gildo Zegna recalls the decision to open Zegna's first China boutique in 1991, when no other luxury apparel maker had entered the country. "We lost money at the beginning," says Zegna, the great-grandson of the founder. But his father and uncles had been selling wholesale fabric to Hong Kong tailors for many years. "They knew there was a huge opportunity," says the CEO, who was educated in Britain and worked for Bloomingdale's in New York before joining the family business. He says the China operations are profitable and have posted 30 percent annual sales growth in recent years.

Still, China was tricky terrain for Zegna. The company had to negotiate store leases with landlords who knew nothing about the luxury business—including the Chinese army, which owned the hotel where Zegna opened its first Beijing outlet. Chinese shoppers preferred stores that were bigger and flashier than Zegna's traditional European-style boutiques, with more-frequent inventory turnover. Zegna's Chinese shops receive six new collections a year, vs. four in the U.S. and Germany. And the company has brought many of its Chinese employees to Italy for training, to ensure they can speak knowledgeably about everything from Zegna family history to the intricacies of Italian tailoring.

Customers are impressed. "This is what a classic suit should look like," says Beijing businessman Wang Jun, fingering an $8,500 worsted-wool suit in Zegna's boutique near the Forbidden City. "Chinese tailors lack the styling,

BRUEDERLE: MICHELE TANTUSSI/BLOOMBERG

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Carly Fiorina wins big in California page 24 ▶



the cutting, and the attention to details that can make your garment a world-class suit." Wang, who is chief financial officer of development company **Beijing Jianxing Group**, says he also shops for clothes in Hong Kong and on London's Savile Row.

Not all luxe menswear purveyors have fared so well in China. **Hugo Boss** closed some stores, including one in Shanghai's trendy Xintiandi district, due to disappointing sales. Analysts say **Giorgio Armani**'s image suffered because some of its midpriced lines, such as Emporio Armani, include items made in China. "The Chinese aspire to European style," says Luca Solca, a Bernstein Research analyst. "If they see it is made in China, they perceive it to be a fake."

As a private company with six family members in its management, Zegna has been able to maintain its investment in China despite recent weakness in the West. Rather than cutting capital spending when the global recession hit in 2007, CEO Zegna says, "We moved it from West to East," speeding the pace of store openings across the mainland. As a result, he says, "We came out of the crisis stronger than other brands."

—*Carol Matlack, with Eugene Tang*

The bottom line *Ermenegildo Zegna, a luxury retailing pioneer in China, is benefiting as growing affluence spurs demand for its pricey menswear.*

Entertainment

Rappers in Search of Quality Street Cred

▶ **Urban recording artists use "hood videos" to bolster their brands**

▶ **"In the underground, these artists can keep their core audience"**

On the cover of a DVD called *Hot Ice*, Curtis Jackson, the Grammy-winning rapper known as 50 Cent, points an automatic weapon at the camera. He does not look happy, despite the bikini-clad model behind him.

During an interview shown on the video, Jackson describes a recent run-in with a rival rapper: "I hit him. But I hit him 'cause what he was sayin' was tellin' me to hit him." Later he details how he took the rival rapper's jewelry. Boasts Jackson, who owns boxer Mike Tyson's former Connecticut estate and has a net worth estimated at up to $100 million: "He ended up giving me two watches in order to get the chain back."

No, this isn't the Barbara Walters interview. Rather, it's part of an edgier underground scene playing out in the storefronts of New York, Los Angeles, and Chicago, and on **News Corp.**'s MySpace social networking site, where reality-based DVDs featuring raw versions of songs and uncensored interviews are promoted and sold. A network of small-time filmmakers cranks out these "hood videos"–productions spiced with the cars, ganja, guns, and girls that characterize the genre.

For the rappers, it's a way to retain credibility with their most dedicated fans and settle scores. The record labels often supply music for the gritty videos gratis because it helps sell their mainstream releases. "In the underground, these artists can keep their core audience," says Ronald Branch, owner of **Sub O Entertainment**, a New York-based video producer. "They can show how tough they really are. 50 Cent can't curse on TV, so he can't really be 50 Cent. So he may be on Jay Leno tonight and in the 'hood with me being a gangster the next day."

Playing to both audiences makes smart business sense. 50 Cent has sold more than 20 million records for the **Interscope Records** unit of Vivendi's **Universal Music Group.** Dwayne Michael Carter, better known as Lil Wayne, a multiplatinum-selling rapper who records for Universal's Cash Money Records label, and Shawn "Jay-Z" Carter, one of the music industry's best-selling stars, have also appeared in hood videos. Carter is signed to a **Live Nation Worldwide** recording, touring, and producing deal; that music will be distributed by **Sony Music Entertainment**.

The record labels don't produce these videos or make any money off them, says James Lopez, a senior vice-president for marketing and brand partnership at Atlantic Records, owned by **Warner Music Group.** "For some of my



Corporate Taxes

Who Pays Uncle Sam the Most—And the Least

Rather than using the "effective tax rate" companies calculate in their earnings reports, the Bloomberg Corporate Tax Ranking tracks total cash taxes paid by S&P 500 companies as a percentage of pretax income between 2005 and 2009 to calculate a real-world tax bite.

The Highest Five-Year Tax Rate	
Freeport-McMoRan Copper & Gold	236.9%
Macy's	214.5%
Goodyear Tire & Rubber	177.5%
Tyson Foods	159.0%
Janus Capital Group	155.8%

The Lowest Five-Year Tax Rate	
Range Resources	0.5%
MetroPCS Communications	0.8%
Carnival	1.1%
Western Digital	1.6%
Plum Creek Timber	1.6%

Who Paid the Most Cash in 2009? (in millions)	
ExxonMobil	$15,427
Chevron	$7,537
ConocoPhillips	$6,641
Microsoft	$6,600
Wal-Mart Stores	$6,596

Who Paid the Least Cash in 2009? (in millions) *	
Allstate	-$1,250
PNC Financial Services Group	-$652
Duke Energy	-$419
PG&E	-$359
Boeing	-$198

*NEGATIVE NUMBERS ARE TAX CREDITS OR REFUNDS
DATA: BLOOMBERG

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artists who have reached a certain level, I really don't want to see them in those things," Lopez said in an interview. In other cases, the videos "are good promotional vehicles."

The DVDs also help record labels find new talent. One hot new artist, Onika Tanya Maraj, who records as Nicki Minaj, was discovered on an underground video called *The Come Up* and signed last year with Young Money Entertainment, a label distributed by Universal Motown.

Many record labels provide the entrepreneurs-cum-filmmakers with upcoming songs as well as uncensored versions of released material, says Sub O's Branch. The videos help promote the music at a time when music industry revenue has fallen dramatically, he says. "It's hard to make money selling records, so they're using these videos to increase sales," says Cathy Jones, who ran Threat Records, a defunct recording label that was affiliated with the rap group Wu-Tang Clan.

With names like *Smack*, *Cocaine City*, and *Trapstar* (slang for a person especially adept at selling drugs), the DVDs sell for $8 to $15 each, and can be found at independent video and convenience stores in urban areas and on Internet sites. Highlights are featured on hip-hop websites, and many of the filmmakers use pages on MySpace to promote and sell them. A MySpace spokeswoman declined to comment.

The productions can be as raw as the streets that give rise to many of the artists. In one, Mario Mims, a rap artist who records on Sony's J Records label under the name of "Yo Gotti," brandishes automatic weapons and appears to be preparing packets of a substance that appears to be crack cocaine. The video is part of a DVD called *Cocaine Muzik*, produced by Dirty Money Films. The company could not be reached for comment.

Producer Branch, whose videos have also featured cameos by sports figures such as NBA All-Star Vince Carter, says the DVDs are in demand because they show a side of urban life often ignored in mainstream media. "Whatever gets blocked creates a vacuum," he says. "And that's an opportunity." B —*Brett Pulley*

***The bottom line** So-called hood videos showcase the rough edges of urban music. Record labels go along, thankful for the marketing help.*

In brief



Snack wraps, smoothies, and Frappes are fueling sales at Mickey D's

McDonald's
Profiting From Snack Attacks

McDonald's global sales growth exceeded expectations in May, powered by new menu items such as Frappes, smoothies, and snack wraps. Sales at restaurants open at least 13 months rose 4.8 percent, the company reported on June 8. Analysts had projected a 4.5 percent bump, according to estimates compiled by Bloomberg. The latest results are proof that McDonald's efforts to boost restaurant traffic outside the traditional lunch and dinner hours are succeeding.

Bank of America
Hit Rewind on Expansion Overseas

Bank of America will pocket $2.5 billion from the sale of a minority stake in Mexico's third-largest bank. Santander is buying back a 24.9 percent holding in its Mexican unit it sold for $1.6 billion in 2003. Back then the Spanish lender was unloading assets in Latin America and Europe to offset losses caused by Argentina's debt default and a plunge in Brazil's currency. Now it's BofA's turn to retrench. The Charlotte (N.C.)-based institution pledged to sell assets as a condition of a $45 billion bailout. BofA announced plans to cash out of Brazil's Banco Itaú last month.

Airbus
Orders for the A380 Are Gaining Altitude

On June 8, Emirates Airline announced it had placed an order for 32 A380s, bringing its total fleet of the Airbus superjumbos to 90. The order, Airbus' biggest to date, is valued at $11.5 billion. Boeing's archrival can sure use the business. Deliveries of the world's largest plane, which seats up to 800 passengers, are running way behind schedule, and the A380 is still years away from becoming profitable.



Foster's Group
The Chinese Have a Taste For Aussie Brews

Tsingtao Brewery and Bright Food Group of China may bid for Foster's Group beer and wine units. The Australian company said last month it plans to split the two into separate companies in 2011. Foster's brewery commands about half the Australian market, with brands including its namesake lager and Victoria Bitter, and could be worth more than $9.8 billion, according to analysts' estimates. The wine business, the world's second-largest, may fetch as much as $3.3 billion. Tsingtao has expressed interest in the beer division, according to the Beijing-based *Economic Observer*. Shanghai-based Bright Food is looking at both of Foster's units, says the *Australian Financial Review*.

Microsoft
A Securities Sale Could Kick-Start a Market

Microsoft's June 9 sale of $1.1 billion of convertible notes may help the market for such paper rebound from a two-month slump. Sales in the U.S. of debt that can be exchanged for stock fell 41 percent in May, to $2.2 billion, from this year's peak in March. Yet there is pent-up demand for investment-grade convertible bonds, say bankers. Buyers of Microsoft's three-year, zero-coupon notes can swap them for shares if the stock rises 33 percent from its current price.

Rosatom
A Russian Nuclear Player Looks West

Russia's Rosatom is paying $610 million for a controlling stake in Uranium One, a Canadian company that has assets in Russia, the U.S., and Australia. State-owned Rosatom needs to tap new sources of uranium to fuel its international expansion plans. The company is in talks to build nuclear power plants in Armenia, the Czech Republic, Egypt, Vietnam, and Venezuela.

Sprint
The Mobile Carrier Needs A Hit Handset

Sprint announced that its new HTC Evo 4G handset broke the company's one-day sales record on its June 4 debut. The carrier did not provide figures, but independent reports peg the day's sales at 320,000. Sprint is counting on the Evo, which costs $199 with a two-year contract, to keep subscribers from defecting to rivals. More than half a million did so last quarter.



ESL Partners
Eddie Lampert May Dodge a Tax Bullet

Billionaire Edward Lampert (below) may have found a way to shield himself from millions of dollars in taxes under legislation that would raise levies on profits at private equity firms. Lampert's ESL Partners and affiliates distributed about $829 million of stock in Sears Holdings, AutoNation, and AutoZone to him on June 2, according to regulatory filings. By taking direct ownership of the shares, Lampert will be taxed at the capital-gains rate of 15 percent when the stock is sold. That is far less than his fund would have to pay under the bill. Documents filed with the SEC described the transfers as "an internal restructuring."



CLOCKWISE FROM TOP: GRAHAM BARCLAY/BLOOMBERG; COURTESY SPRINT; GREGORY BULL/ AP PHOTO; JACK ATLEY/BLOOMBERG

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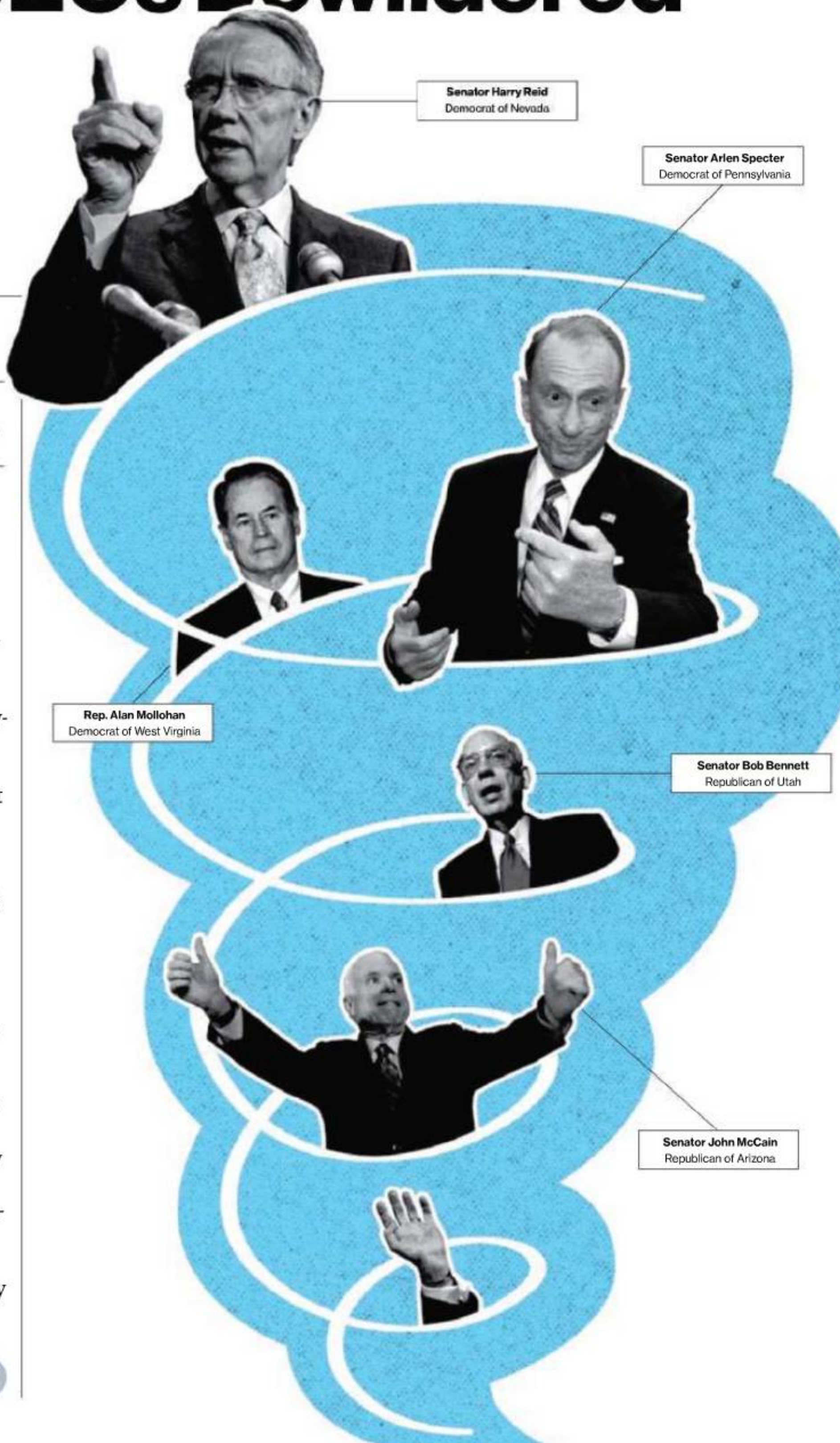
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Politics&Policy

A Wild Political Season Leaves CEOs Bewildered



▶ Business leaders contend with a climate of chaos

▶ "This kind of extremism makes it much harder to plan"

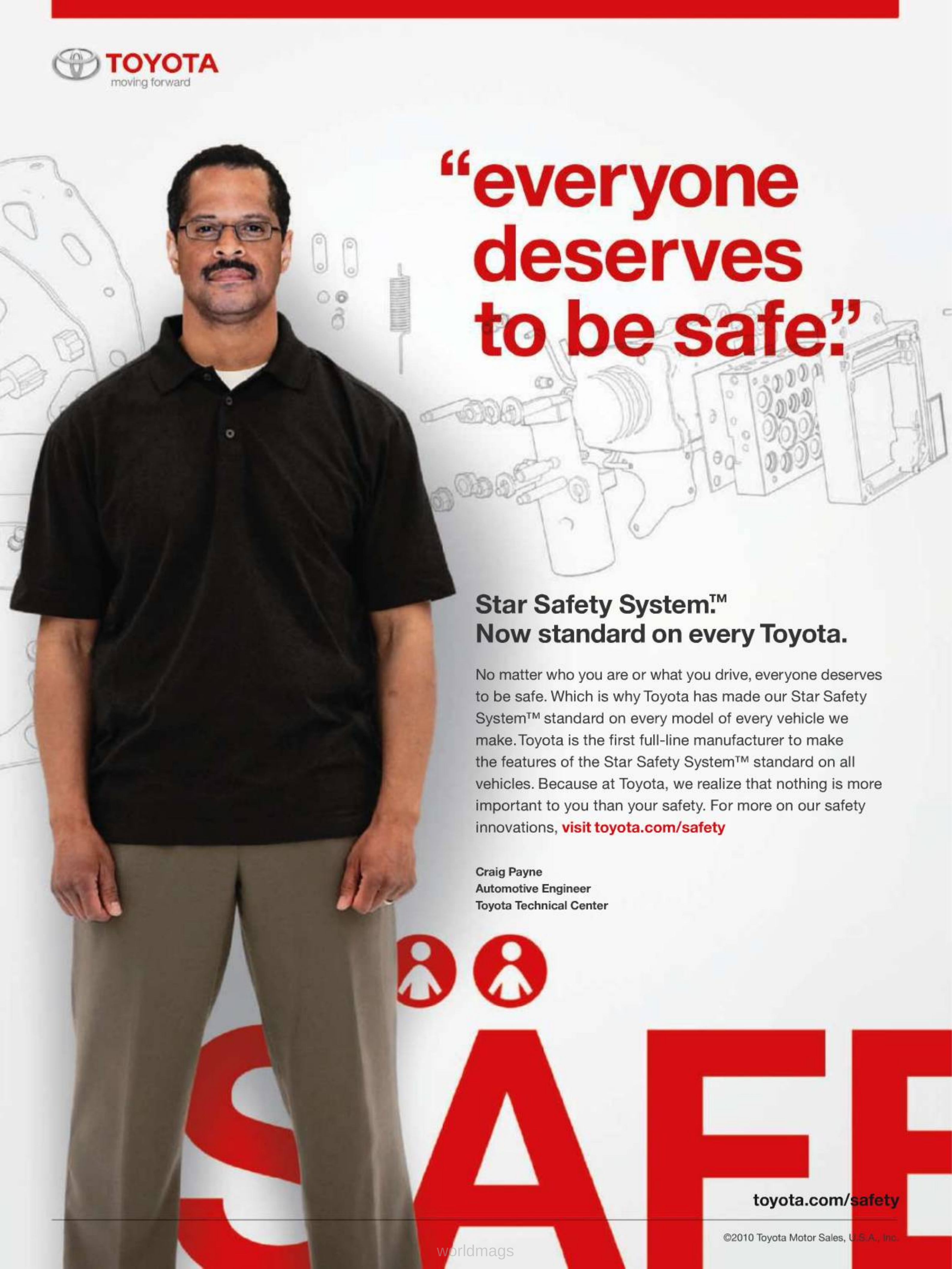
Incumbency used to be a reliable predictor of electoral success. Not this time around. The primaries, run-offs, and special elections held in 12 states on June 8 provided fresh evidence that this is going to be a raucous, rebellious political season. Neither party is in control, given the level of public disenchantment over the economy and the Washington Establishment. Veteran lawmakers, the recipients of long-running investments by lobbyists and business leaders, have been swept out of office at a dizzying pace.

For business leaders, the result is a climate of chaos that denies them the certainty they crave. No one knows this better than Ralph Izzo, the chief executive officer of **Public Service Enterprise Group**, New Jersey's largest utility. "The big unknown is whether or not Congress will take action on carbon dioxide," says Izzo. "Absent clear environmental regulations, your long-term strategy is something you really have to equivocate on."

Energy policy is by no means the only great unknown. Taxes, trade, immigration, jobs programs, and runaway entitlements—to name just a handful of major issues pending in Congress—all hinge on who controls the levers of power. Already trying to absorb what the new health-care law and soon-to-be-passed financial regulation reforms might do to profits, executives nationwide don't

ILLUSTRATION BY CHRISTOPHER BRAND. FROM TOP: ROLL CALL/GETTY IMAGES; GETTY IMAGES (2); AFP/GETTY IMAGES; GETTY IMAGES; CQ/GETTY IMAGES

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TOYOTA
moving forward
"everyone deserves to be safe."
Star Safety System.™
Now standard on every Toyota.
No matter who you are or what you drive, everyone deserves to be safe. Which is why Toyota has made our Star Safety System™ standard on every model of every vehicle we make. Toyota is the first full-line manufacturer to make the features of the Star Safety System™ standard on all vehicles. Because at Toyota, we realize that nothing is more important to you than your safety. For more on our safety innovations, visit toyota.com/safety
Craig Payne
Automotive Engineer
Toyota Technical Center
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Asustek's offbeat iPad strategy page 31 ▶



know when, or if, Congress will move on any of the other high-stakes issues.

The only discernible trend from the latest primary results is that women won big, though money or Tea Party backing seemed to matter more than gender. In California, former **Hewlett-Packard** CEO Carly Fiorina was chosen by state Republicans to face Democratic Senator Barbara Boxer this fall. Meg Whitman, the former **eBay** chief who spent $71 million of her own money on the Republican gubernatorial primary, triumphed and will face Jerry Brown, a former governor, in November.

In Nevada, Sharron Angle, a candidate backed by Tea Party activists, beat two establishment Republicans and will square off against Senator Harry Reid, the majority leader and a top Republican target. Senator Blanche Lincoln of Arkansas narrowly survived a Democratic primary challenge from the left, though she will face an even bigger challenge this fall against Republican Representative John Boozman, who now enjoys a 20-point lead in the polls.

Some of the June 8 wins make business leaders nervous, for fear that both parties are moving to ideological extremes. Angle, for example, opposes

The June 8 results are raising business leaders' fears that both parties are moving to extremes

funding for Obama's health-care law, wants the Education Dept. eliminated, and has called for the current tax code to be scrapped—views shared by many Tea Party activists. "This kind of extremism makes it much harder to plan from a business perspective," says John Castellani, chief executive officer of the Business Roundtable.

Castellani describes a record level of anxiety among his member CEOs, more than 70 of whom attended a quarterly meeting last week, while 90 participated in February, the largest turnout in his decade with the business group. His members, nearly all heads of multinational corporations, are particularly concerned about stalled free-trade agreements and new taxes on foreign income. "People are trying to discern what the trends are," he says. "Are these candidates who are going to understand that 95 percent of the world lives outside the United States, or isolationists?"

William Lane, Washington director for **Caterpillar**, watched the Arkansas race closely. The world's largest maker of construction equipment backed Lincoln, the chairwoman of the Senate Agriculture Committee and someone known to champion the agribusinesses Caterpillar sells to, because she is a "probusiness" Democrat, says Lane. "None of us knows whether Republicans are going to have moderate success, significant success, or historic success," Lane says. "But one thing that is clear is that the Congress is going to be recentered after November."

If that's the case, Lane sees a silver lining, predicting that business will be able to play a greater role in shaping policy amid an environment where the parties may be even more inclined to appease their respective bases. "Business is going to have a unique role to play, and it's just absolutely critical that it plays that role," he says.

For Lewis Hay, CEO of Juno Beach (Fla.)-based **NextEra Energy**, the largest renewable energy producer in North America, the results of individual races are less important than what party controls Congress—and gets the power to set the agenda. "One senator from Florida isn't going to impact what we do in Florida very much, but the composition of the House and the Senate could very well have an impact," he says.

Hay is following what he calls a "no regrets" investment strategy for NextEra. If Congress passes legislation setting a national mandate for alternative energy sources like wind and solar, those industries will prove to be "very, very good investments," Hay says. If Congress fails to act, the investments will still be good, although definitely less profitable. "We would clearly invest a lot more, with more clarity on our climate and energy policy," he says. "There's a lot of capital sitting on the sidelines."

While he hasn't started tracking exit polls—at least not yet—Izzo is closely monitoring elections in regions where PSEG operates and other major races. "I'm a little more worried about how things change post-November than before," he says. "Each day Congress waits puts us a little bit more behind."

—*Lisa Lerer and John McCormick*

The bottom line *The exodus of veteran lawmakers vexes companies and lobbyists hoping to shape tax, energy, and regulatory policies in the months ahead.*

Tea Party Winners



Sharron Angle

Nevada Senate

Tea Party activism propelled the former state lawmaker past two GOP rivals in a hotly contested primary; now faces Senate Majority Leader Harry Reid.



Carly Fiorina

California Senate

The former Hewlett-Packard CEO moved right to win Sarah Palin's endorsement and the GOP Senate primary; faces Democratic incumbent Barbara Boxer.



Marco Rubio

Florida Senate

Strong Tea Party support for Rubio forced Governor Charlie Crist to run as an independent, making Rubio the likely GOP Senate nominee.



Rand Paul

Kentucky Senate

Rode a wave of Tea Party support to win Republican primary for open Senate seat, beating opponent endorsed by GOP party leaders.

Incumbent Losers



Bob Bennett

Utah Senate

Three-term Republican senator lost party's nod to run for a fourth term at a state convention dominated by Tea Party activists.



Parker Griffith

Alabama House

The first-termer, an Alabama Democrat-turned-Republican, lost his June 1 primary to a lesser-known county commissioner with Tea Party support.



Alan Mollohan

West Virginia House

The 28-year Democratic congressman lost a primary last month, after opponent Mike Oliverio tapped voters' strong anti-incumbent mood.



Arlen Specter

Pennsylvania Senate

After switching from the GOP to the Democratic Party, 30-year Senate veteran was defeated by Representative Joe Sestak in a closely watched primary.

CHART: TOP ROW, FROM LEFT: AP PHOTO; ORANGE COUNTY REGISTER/ZUMA PRESS; VIVIAN RONAY/ZUMA PRESS; ROLL CALL/GETTY IMAGES. BOTTOM ROW, FROM LEFT: UPPA/ZUMA PRESS; ROLL CALL/NEWSCOM; CQ/GETTY IMAGES; EPA/CORBIS

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Edwards got a loan through Prosper that a bank likely wouldn't make

Regulation

An Online Lender Takes On the SEC

▶ Prosper says it shouldn't be treated like an investment firm

▶ "Investors are entitled to ... full and fair disclosure," says the SEC

In 2006, Chris Larsen started **Prosper Marketplace**, an online service where borrowers apply for loans of up to $25,000 and individual investors bid to lend as little as $25. Soon he was at war with the Securities & Exchange Commission, which insists that Prosper is an investment firm offering bonds, and not a lender.

Larsen disagrees, arguing that the SEC "is putting a round peg into a square hole" as it applies securities laws dating from the 1930s to the Silicon Valley startup and other so-called peer-to-peer lenders. By the middle of 2009, Prosper had spent $4 million, even shutting down for nine months, to comply with SEC rules. Larsen claims the company now spends more than $1 million annually on legal fees and audits, and makes more public disclosures–about two a day–than almost any other company. The filings include details on each potential borrower's credit score and why they need the money.

Prosper isn't arguing against all regulation, just regulation by the SEC. The company wants to be overseen by the consumer financial protection agency Congress may soon create. Larsen, 49, argues that by trying to twist the industry into something it's not, the SEC is harming innovation and shutting off a source of credit for small businesses as the economy struggles and traditional banks lend less.

Israel Klein of the **Podesta Group**, Prosper's lobbyist, last year persuaded the House to place the nascent industry under the jurisdiction of the new consumer agency, part of the financial regulation bill. The SEC, after getting wind of the move, blocked a similar provision in the Senate measure. John Nester, an SEC spokesman, says the agency had a duty to protect investors. "Regardless of the innovative way in which investments are solicited, investors are entitled to the full and fair disclosure that our securities laws require," he says.

Based in San Francisco, Prosper is one of two major U.S. peer-lenders; it employs about 30 people. Since its launch, the service has originated $197 million in loans. Its main competitor, **Lending Club**, which isn't fighting with the SEC, has issued $121 million in loans. Research firm Gartner predicted in January that peer-to-peer lending will jump at least 66 percent, to $5 billion, in outstanding loans by 2013.

Priscilla Edwards turned to Prosper last year to help her publish a children's book about a tugboat on San Francisco Bay. Edwards, 62, read about Prosper in the local paper, then went online and borrowed $10,000 at a 13.9 percent interest rate from 141 people, having attracted bids from 391 potential lenders. "Never in a million years" would a bank loan her money, Edwards says, noting she had no collateral.

Some securities lawyers agree with the SEC. "When you're talking about loans of hundreds of dollars ... the antenna goes up," says Donald Langevoort, who teaches securities law at Georgetown University. "It means you are targeting very unsophisticated people."

To Larsen, the disagreement is symptomatic of a deep divide between Washington and Silicon Valley. "I'd really like to see Mary Schapiro out at Stanford, at Harvard, encouraging startups," Larsen says, referring to the SEC chairman. "It's not a welcome environment for entrepreneurs."

—*Robert Schmidt and Jesse Westbrook*

The bottom line *The SEC's insistence that securities laws should apply to online lending services has set off a fight about innovation and regulation.*

Labor Unions

Nurses: Fed Up and Not Taking It Anymore



▶ Big work stoppages crop up over proposed pension and staff cuts

▶ Hospitals' relations with nursing staff is "hitting the boiling point"

Hospitals coping with shrunken state budgets and anticipating cuts from President Barack Obama's health-care overhaul are now getting squeezed by a new power: an activist nurses union.

Twelve thousand members of the National Nurses United (NNU) planned a one-day strike on June 10 in Minnesota, the biggest work stoppage ever by U.S. nurses, the union claimed. (A San Francisco court order on June 8 barred another walkout set for the same

FROM TOP: PHOTOGRAPH BY ROBYN TWOMEY FOR BLOOMBERG BUSINESSWEEK; MATT ROURKE/AP PHOTO

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Speed Dial

A Culture War Brews



A chat with American Enterprise Institute President Arthur C. Brooks, who's giving voice to the Tea Party movement in speeches, op-eds, and a new book

You say the next culture war will be over European-style government vs. the free enterprise system. What's the evidence?
No matter how you slice and dice the [polling] data, about 70 percent of Americans say the free enterprise system is best for the U.S. They see it as a pillar of American culture; it's central to who we are. So when a minority starts to impose a cultural change on a majority, you get a great big backlash. Tea Partiers are an example.

What's wrong with European social democracies?
What brings greater sense of fairness and happiness to people is the belief they have earned their success. If government redistributes money, you will get more income equality but you won't get more happiness. It's a statistical fact.

Some argue that free enterprise failed miserably and that Washington must now correct the excesses.
Free enterprise is not the same as being a shill for big business. Big business has a Faustian tendency to crawl into bed with government. The engine of growth in this country is entrepreneurs. The free enterprise system didn't fail us in the financial crisis. The root of the problem was government housing policy.

Are you opposed to regulation per se?
No, I'm in favor of smart regulation. What I'm against are bailouts that shield people from accountability and don't let companies like GM and Chrysler go bankrupt in an orderly fashion; social engineering like Fannie Mae and Freddie Mac, which gives people incentives to take out mortgages they don't deserve and can't afford because [the government] feels everyone should own a home; and pork-barrel spending like cash for clunkers because the government's now in the car business.

Should Obama have let banks and auto companies fail?
If I could wind back time, I would say never do bailouts. But by the time we were doing bank bailouts, the die was cast. We didn't understand very well what the danger was, so the pragmatic policy, particularly by the [Federal Reserve], was probably the way to go. In the case of the car companies, that was indefensible.

It's not important to have a domestic auto industry?
That's how creative destruction works. I would have preferred the auto companies not to have made bad management and labor errors.

You say public sector unions are bankrupting the country. Are you prepared to go to war with the labor movement?
All you have to do is look at the unfunded pension liabilities and the disparity of benefits that accrue to public sector employees compared to the private sector. The disparity is so large and so unfair, a day of reckoning is coming. B
—Paula Dwyer

day at University of California hospitals.) Last month 1,500 members at an NNU affiliate in Philadelphia stopped work for a month, ultimately winning concessions.

The union's assertiveness could hamper efforts to slow exploding health-care costs, which rose 5.7 percent last year, to $2.5 trillion. Hospitals are slated to bear the brunt—$113 billion—of the $196 billion in savings mandated by Obamacare over the next decade, according to the Congressional Budget Office. That may be hard if the nurses' union insists on staffing increases.

The 150,000-member NNU, formed in December from various state nurses associations, has made mandatory hospital nurse-to-patient ratios its main agenda item. California is the only state with such a law. Cuts in staffing "have always been bad, but the cuts the last two years have made it even worse," says John Nemo, a spokesman for the NNU's Minnesota Nurses Assn.

The labor strife reflects state financial woes and hospitals' attempts to respond to the federal health-care law, which will boost insurance rolls but also seeks to reduce costs, including those for Medicare, the federal health-care program for the elderly. Cuts in Minnesota's health budget reduced state payments to hospitals for patient services under Medicaid or other programs beginning in 2009. "Hospitals are thinking ahead, they know that they will not be getting as large Medicare payment updates in the future," says Jean Abraham, an assistant professor of health policy at the University of Minnesota in Minneapolis. In Minnesota, the NNU affiliate is calling for guaranteed nurse-to-patient ratios, maintenance of employer pension contributions, and annual raises as high as 4 percent over a three-year contract.

The 14 targeted Twin Cities Hospitals want cuts of about 30 percent in pension contributions after being forced to double contributions this year to pay projected benefits. They also want more staffing flexibility, and raises of less than half what the union is seeking. The Minnesota nurses' staffing proposal would leave hospitals paying $250 million more a year for labor, says Maureen Schriner, a spokeswoman for the hospitals. "They think we can just increase our costs because we can just pass that cost on to our payers, but that's just

PHOTOGRAPH BY MATT EICH FOR BLOOMBERG BUSINESSWEEK

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from a bygone era," Schriner says.

Tensions between health-care institutions and employees are "hitting a boiling point" in many states, says Eric Simon, a partner at law firm Jackson Lewis who represents health-care employers in New York. "Revenues are becoming tighter, [and] the areas for finding common ground are becoming more and more difficult to achieve."
—*Dune Lawrence*

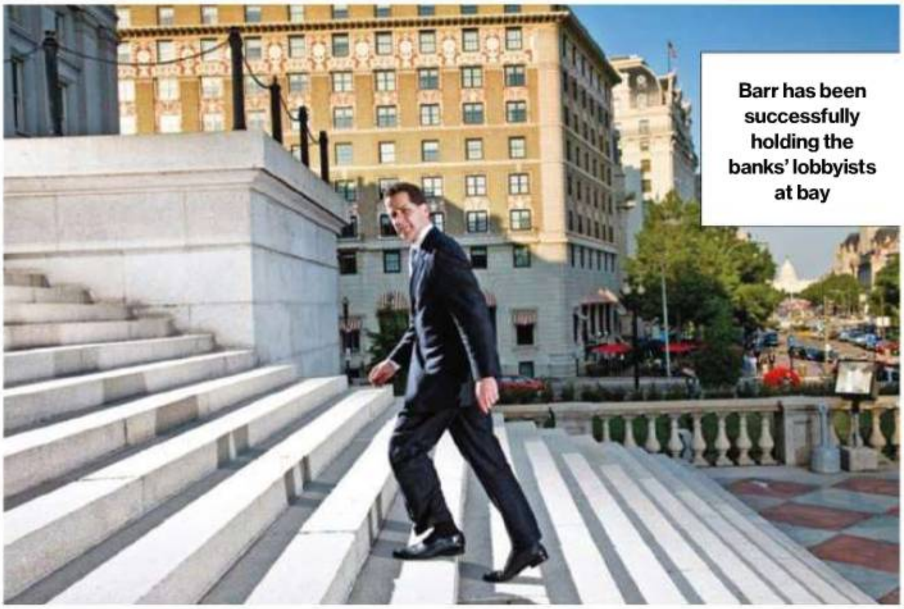
The bottom line *Hospitals and a new nurses' union are taking a tough line on salaries and benefits now, in advance of the cost pressures from Obamacare.*

Financial Oversight

Wall Street Can't Beat Its Nemesis at Treasury

▶ **In talks with banks over regulation, Michael Barr has stayed tough**

▶ **"That we don't always agree with lobbyists is a good thing"**



Barr has been successfully holding the banks' lobbyists at bay

When banks and their Washington lobbyists try to assign blame for the thrashing they've taken in the battle over financial regulation, one name usually comes up: Michael S. Barr.

The 44-year-old assistant Treasury secretary is one of several Administration officials charged with pushing the overhaul measure to final passage, expected in the coming weeks. A law professor and devotee of behavioral economics, Barr has championed policies especially disliked by Wall Street, including the creation of a consumer financial protection agency and the so-called Volcker Rule prohibiting banks from trading for their own accounts. "Our view is that he doesn't understand the industry very well, doesn't have a background with the industry, and has a philosophy that is inimical to free enterprise," says Wayne Abernathy, executive vice-president of the American Bankers Assn.

Barr agrees his relationship with the industry can be prickly. "They have just come off a period of time where they wrote the legislation and the [Bush] Administration literally invited them into the closed room to cut deals, and that's not the way we work," he says. "The fact that we don't always agree with the lobbyists is not a bad thing."

Barr is helping lead the search for people to run the consumer protection unit and the regulatory agency for national banks. The industry fears Barr will make himself the top choice for one of the posts, most likely the consumer protection job, says Abernathy, who held Barr's position in the George W. Bush Administration. Barr declined to discuss his future.

Advocates of tougher financial regulation credit Barr with helping to preserve the consumer agency's independence, which almost became a casualty during Senate negotiations. "There are many reasons why that doomsday scenario has not played out, but Michael Barr is one of the very significant reasons," says Travis Plunkett, legislative director for the Consumer Federation of America.

Banks found him to be an implacable adversary, even when they sought a compromise on the provision of the Volcker Rule that bars them from owning hedge funds. First banks tried to get a 10 percent ownership cap, then 5 percent; they threw in the towel when Barr rejected even 3 percent.

Barr envisions the consumer agency as a laboratory for ideas derived from behavioral economics, which seeks to steer consumer or corporate decisions in the direction the government wants by blending psychology and economics. Bankers and Republicans complain that the theories are a cover for Democrats' predilection to interfere with the free market. Barr says that consumers with access to risk and reward information make better choices, so government can be less intrusive. "A lot of the effort is built around having better information, using empirical data to understand how people actually think and behave," he says.

On leave from the University of Michigan, and with his wife and three children at home in Ann Arbor, Barr's life in Washington revolves around the congressional schedule and the bill. He sometimes holds midnight staff meetings and heads home every weekend. "We are going to get a bill and it's going to be a good bill," he insists. "But the margin between that and just nailing it is what I'm focused on now. And I like nailing things." —*Robert Schmidt*

The bottom line *Barr hopes the consumer financial agency becomes a laboratory for testing the theories of behavioral economics.*

Quoted

"We talk to these folks because they potentially have the best answers, so I know whose ass to kick."
—President Barack Obama, on NBC's *Today* show June 8, explaining why, in three trips to the Gulf of Mexico, he speaks to fishermen and others affected by the Gulf oil spill

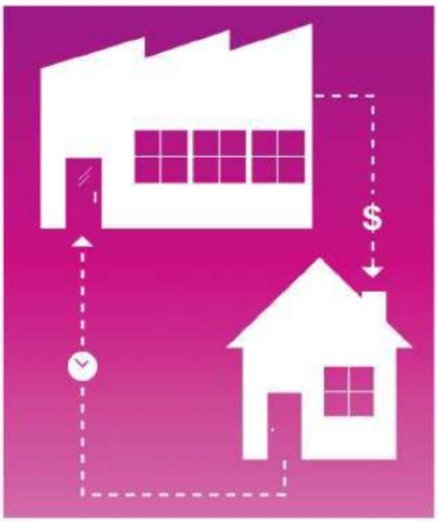


FROM TOP: PHOTOGRAPH BY ANDREW CUTRARO FOR BLOOMBERG BUSINESSWEEK; GETTY IMAGES

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James Warren

It Pays to Help Workers Buy a Home



A slew of new programs offer employees the chance to purchase a house with company assistance. It's more than a nice gesture—it's a cost-saver, too

Maria Garza lives in a high-rise condo on Chicago's swish North Side. Virginia Johnson, a joiner-insulator for Northrop Grumman Shipbuilding, loves her three-bedroom home in rural Hurley, Miss. Anne Kingston heads to her manager's job at a CVS pharmacy in downtown Washington from a duplex in Temple Hills, Md. All three owe their homes to their employers–and not simply because they pay their salaries. Each company saw a low-cost, high-reward link between home ownership, proximity to the job, and a productive workforce.

Seems obvious, right? Help educate a worker about home ownership, counseling them on improving their credit if they've got problems. Steer them toward nearby, affordable neighborhoods with dependable public transit, perhaps improving the 'hood in the process. Assist with a down payment or closing costs, forgiving the de facto loan if they remain with the company for a certain period. It's a shrewd way to increase rank-and-file worker commitment at a modest price by supporting a significant moment in life: buying a home. "This is not about community relations. It's a business decision, and it's not expensive to administer," says Stephen Wing, director of Workforce Initiatives at Woonsocket (R.I.)-based CVS Caremark. Although he won't cite a cost figure, Wing insists that "this keeps people employed and helps in retention."

More than 100 CVS Caremark employees in Washington, Los Angeles, and Orange County, Calif., have bought homes through the program since it began in 2005. Not one has been through foreclosure or left the company. The typical CVS beneficiary earns between $30,000 and $50,000 and, after expressing interest to a manager, gets free counseling on home buying and credit at a CVS learning center staffed by a local faith-based organization. Reliance on churches isn't outsourcing, it's strategic; especially in big cities, many CVS employees don't trust banks and don't want the company to know much about their finances. They're encouraged to purchase homes within walking distance of the branch where they work or close to mass transit, and they receive a $1,000 check at closing that can be used for moving, a new dishwasher, or anything the employee wants. Garza got $8,000 from Loyola University, while Northrop Grumman's Johnson received a total of $30,000 in company and state aid.

CVS will soon move its home ownership program to the south suburbs of Chicago, where benefits will be greater due to state assistance. Indeed, Chicago is the capital of employer-assisted housing. In 2000, the nonprofit Metropolitan Planning Council piloted a program with System Sensor, a maker of smoke detectors and sprinklers in upscale St. Charles, Ill., aimed at keeping workers within a closer radius of the plant. System Sensor offered free real estate and credit counseling and a $5,000 down payment on a purchase. If a worker stayed with the company five years, the loan was forgiven. The nonprofit and its corporate partner, now a division of Honeywell International, later convinced the state to implement incentives for employers; a $5,000 state match for each home purchase and a tax credit of 50¢ on the dollar to employers on the down payment, counseling, and administration. Over 50 Illinois employers, including Charter One Bank, Rush University Medical Center, and the Chicago Public School system take advantage.

Most large companies offer relocation assistance to top executives; few bother with housing for the rank and file. Northrop Grumman is an exception; 77 employees at Northrop Grumman Shipbuilding closed on a first home or replaced one destroyed by Hurricane Katrina with a $7,500 forgivable loan matched 3 to 1 by the state. Ms. Johnson, 23, got $30,000 to help buy a 1,400-square-foot brick home that's a 20-minute drive from the Pascagoula (Miss.) shipyard. "It wouldn't be possible if it hadn't been for the program and staff," she says.

At Loyola, one must live near a specific Chicago mass transit line because of the university's "green initiative" to cut reliance on cars. Twenty employees, most earning less than $70,000, have closed on homes since 2008. Milwaukee's Aurora Health Care, a 29,000-employee nonprofit with 14 hospitals in Wisconsin, partly wanted to stabilize iffy neighborhoods. It provides a $3,000 forgivable loan to buy in the city. Some 400 employees, including dieticians and nursing assistants, have taken advantage. The Center for Housing Policy in Washington, an independent think tank, concluded in a 2008 study that Aurora's "modest investment" improved productivity and loyalty. It also sharply reduced turnover and, thus, recruitment and training costs. Besides creating long-term cost savings, the CHP study found that the Aurora employees who get housing assistance "are proving to be better-performing employees who choose to stay with the organization longer." Dwight Morgan, Aurora's human resources chief, faces the same cost-cutting pressures as everybody. "But this is a program we're unwilling to change." Ⓑ



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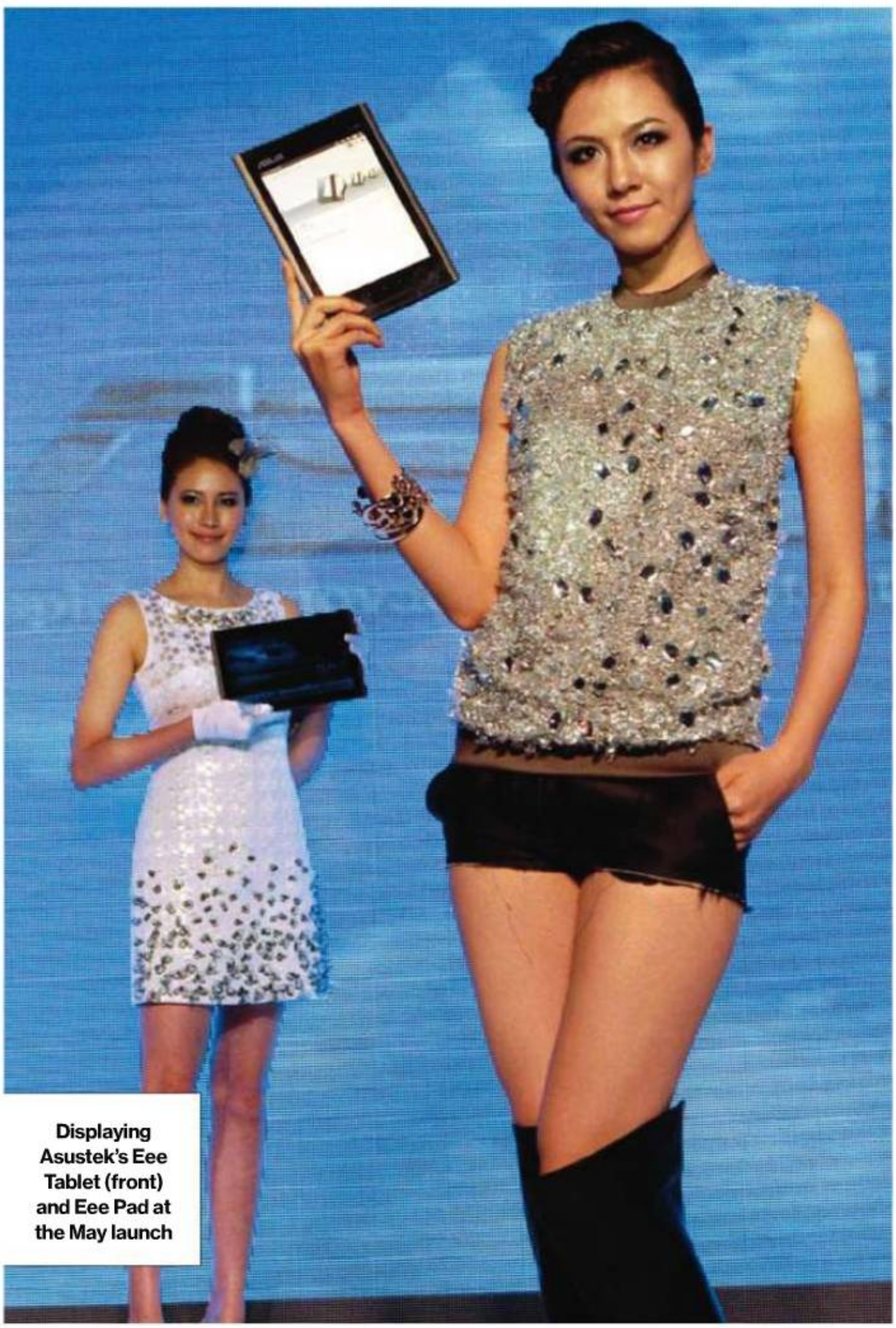
Contents ▶ Why Europe's hit music site hasn't made it to America yet 32 ▶ When Groupon coupons work too well 32
▶ Cloning to save endangered species 34 ▶ A tech solution to parking cheapskates 37 ● Edited by Jim Aley

Technology

A Netbook Pioneer Enters the iPad Age

▶ **Taiwan's Asustek is launching tablets while continuing to push mini-laptops**

▶ **"They have a very good product but the environment is not ready"**



Displaying Asustek's Eee Tablet (front) and Eee Pad at the May launch

IMAGINECHINA/AP PHOTO

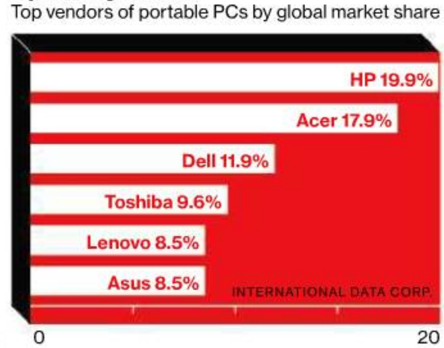
Tiny computers have been good to **Asustek**. The Taiwanese company in 2007 introduced the first netbook, those low-priced mini-laptops that have been the PC industry's fastest-growing product for the past two years. Netbooks now represent nearly 40 percent of the Asus brand's sales and have been the primary factor in helping Asustek tie **Lenovo** as the world's No. 5 portable PC company, according to researcher International Data Corp.

Now it looks like the netbook growth engine is losing steam. Netbooks' share of the global PC market will probably be flat this year at 12 percent, IDC estimates. Instead, consumers are flocking to tablets such as **Apple**'s iPad, which offer many of the advantages of netbooks. For Asustek, that means making a big push into tablets while trying to convince corporations and consumers that there are still advantages to netbooks.

On May 31, Asustek unveiled its first weapons in the battle against the iPad: the Eee Pad and the Eee Tablet. Like Apple's device, the Eee Pad—available next winter—will have a touchscreen, an embedded keyboard, and videoconferencing capability. Unlike the iPad, the Asus machine will sport an

Upwardly Mobile

Top vendors of portable PCs by global market share



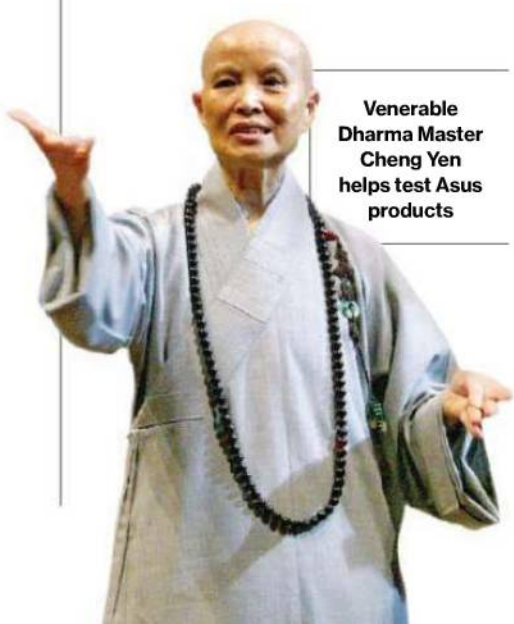
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Technology

Intel processor and use the Windows 7 operating system. The Eee Tablet, to hit the market in early 2011, is an electronic book reader with a touchscreen and built-in camera that allows users to write notes on photos. The new gadgets could be "key drivers for Asustek's sales and earnings growth in the coming years," KGI Securities analyst Angela Hsiang wrote in a June 1 report.

Asustek will have plenty of competition, even aside from the iPad. **Dell** has introduced a mini-tablet called the Streak, and almost every other PC maker has a tablet in the works, though some have delayed launches in the wake of the iPad. While the new Asus machines will hit stores before most of the competition, investors clearly have doubts about Asustek's strategy. Its Taipei-listed shares dropped 18 percent this year through May 17, when stock sales were suspended pending the upcoming spinoff of the company's manufacturing arm. One investor worry is that Asustek can't offer as many apps as Apple can. "They have a very good product but the environment is not ready; there's still not enough content," says Robert Cheng, an analyst in Taipei with Credit Suisse. Another problem is that the Eee Pad will have about six hours of battery life, four hours less than the iPad.

Asustek CEO Jerry Shen believes he still can tap a vast corporate market for netbooks. The company is tinkering with design, moving away from the current clamshell look to sleeker one-piece models–a kind of tablet shape but with a physical keyboard. Asustek "will have a lot of different types of netbooks that can still provide a better user experience" than tablets, says Shen.



Venerable Dharma Master Cheng Yen helps test Asus products

To hedge against a big decline in netbook popularity, Asustek is heading upscale. In May the company launched notebooks with **Bang & Olufsen** sound systems and introduced a line of laptops with bamboo on the lid, using 20 percent less plastic than other machines. "We still have a lot of innovation going on," Chairman Jonney Shih says, showing off the private lab adjacent to his office where he retreats to clear his mind by tinkering with Asus gadgets.

One of Asustek's most offbeat innovations is its product-testing strategy. A Buddhist vegetarian, Shih is a supporter of the Tzu Chi Foundation, one of Taiwan's biggest Buddhist charities. He enlisted Venerable Dharma Master Cheng Yen, the foundation's 73-year-old founder, to help test e-readers. Cheng Yen "is the best quality assurance," Shih says. "She is so patient." As Asustek tries to match the iPad, he'll need patience from customers, too.

—Bruce Einhorn and Tim Culpan

The bottom line *Asustek is working on new tablets as sales of its mainstay machines, tiny netbooks, begin to flatten.*



Spotify founders Daniel Ek and Martin Lorentzon

YEN: UNIONCOM/CHINAFOTOPRESS

Digital Music

Why Europe's Hit Music Site Isn't Playing the U.S.

- **Big labels have blocked Spotify from offering streaming music**
- **The first site that's "sexy without having the Apple name on it"**

Sweden has a new music export, and it's attracting an audience way broader than an ABBA greatest hits album. Twenty-month-old **Spotify** allows listeners to tune in to their favorite music over the Internet. It has 7.7 million registered users across Europe, according to digital media tracker ComScore. That's roughly 10 times the audience of **Rhapsody**, which has been around for nine years and is the leading music subscription service in the U.S.

For more than a year, Spotify's cofounder, Daniel Ek, has been trying to bring the service to the U.S. What's stopping him are the industry's four major record labels, **Universal**, **Sony**, **Warner**, and **EMI**. They have licensed

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their music to Spotify for use in the U.K., Spain, France, Finland, Sweden, Norway, and the Netherlands, where most listeners tune in to the service free. In the U.S., the labels want the service to make them money and help compensate for a 65 percent drop in CD sales over the last decade.

Aside from the free part, the labels like Spotify for the same reason listeners do. Tunes from its 8 million-song catalog load quickly, and listeners can compile playlists of their favorite tracks and gain access to them from any computer. "Spotify is the first digital offering that has come along that people find sexy without having the **Apple** name on it," says Ted Cohen, a former top digital executive at EMI Music, whose Tag Strategic advises companies on digital strategy.

The four big labels want Spotify, now based in London, to junk its free model and find a guaranteed revenue stream it could share with them, say music executives with knowledge of the discussions. Rhapsody and U.S. rivals **eMusic** and **MOG** charge monthly fees. "Free streaming music services are clearly not net positive for the industry," said Edgar Bronfman Jr., chief executive officer of Warner Music Group, during an earnings call in February. Warner was an early investor in Spotify.

The service already offers two premium plans in Europe: For the equivalent of around $6 a month, listeners get unlimited playtime with no ads; $12 buys better sound quality and the ability to play music from a cell phone. So far only 320,000 users have signed up for subscriptions, a sign that Europeans exhibit the same resistance to paying for music that Americans do. For the record labels, clearing that hurdle is crucial as CD sales continue to plummet and Apple's iTunes keeps its grip on digital music pricing. "Nothing in digital has been able to counter the decline in traditional revenue sources," said Ek, 27, at an industry conference in March. Record companies, he said, are "concerned about how to ensure that people don't stop buying CDs."

The major music companies have been pressing Spotify to ally with wireless service providers so they can get a cut of the monthly charges. Spotify has tried that, signing a deal with Swedish telephone operator **Telia**. Plus, it has created apps for the Apple iPhone and handsets powered by **Google**'s Android software.

Google also has been "kicking the tires" at Spotify, according to music executives with knowledge of the search engine's interest, but no acquisition is in the works. Apple bought **Lala**, another music streaming service, last year, only to shut it down at the end of May. The talk in the industry is that Steve Jobs wants to incorporate Lala's technology into a subscription version of iTunes, which would allow listeners to gain access to their music libraries from any device.

Whether Spotify becomes an iTunes competitor will depend on the fickle tastes of consumers. One part of the equation will be whether the music labels let it do business in the U.S.
—*Ronald Grover and Adam Satariano*

The bottom line *The music majors are pressing a hot European startup to dump its free service as a condition for licensing their tunes for use in the U.S..*

Quoted



"I think we coexist quite well with Netflix, but let's face it: *Avatar* comes out, and you want to stream it, you come to me."
—Blockbuster CEO James Keyes in a June 8 *Fast Company* interview. That day Blockbuster was worth $56 million, vs. Netflix at $5.8 billion

KEYES: SHANNON STAPLETON/REUTERS

E-Commerce

Sometimes Groupon Coupons Work Too Well



- **Customer response to the coupon site can overwhelm merchants**
- **"We say to businesses, the first day is going to be crazy"**

Last October, when Philz Coffee offered users of the coupon website Groupon discounted gift cards for in-store pickup, Jacob Jaber, president of the San Francisco coffee chain, figured on a few hundred takers. He got more than 2,000. "I nowhere near projected the amount of people that showed up," says Jaber. "We just weren't prepared for it." He ran out of cards, irritating customers, and says he'll probably stick with word-of-mouth marketing from now on.

Jaber's mishap spotlights a challenge for **Groupon**, a Chicago-based startup that has sold nearly 6 million online coupons since its founding in 2008: Sometimes it works too well. Groupon offers users a daily deal at local establishments ranging from restaurants and shops to skydiving operations and spas. It works with businesses in more than 140 cities in 18 countries. When Groupon posts an offer on its site, it keeps 50 percent

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Technology

Why analysts are too optimistic 38 ▶

60

MILLON

U.S. households with 3D-capable TV sets by 2014. By the end of this year the number will be about 2.5 million.

DATA: FUTURESOURCE CONSULTING

of the revenue. The local merchants can set a cap on how much they want to sell. The trouble is, those businesses don't always make the cap low enough and get overwhelmed by bargain-seeking hordes. A nail salon in Boston sold 4,000 manicures and pedicures before Groupon discovered the shop had just two stations to serve customers, says Andrew Mason, Groupon's founder and chief executive officer.

Privately held Groupon, which declined to comment on its financials, says it aims to double its U.S. coverage to 100 cities this year. In April the startup got $135 million in funding from **Digital Sky Technologies**, the Russian investment firm that also owns as much as 10 percent of Facebook. The risk from disgruntled customers is lawsuits, says Jeremiah Owyang, an analyst at research firm Altimeter Group. "Imagine you're a consumer and you didn't get the manicure or pedicure you paid for," he says. "Who do you sue, the small business owner or someone who just got $135 million?" Mason says Groupon hasn't been sued for unfulfilled deals, and adds that the company offers customers full refunds if they're dissatisfied. In the coming months, he plans to add online marketing seminars to better prepare small business owners for spikes in demand. "We say to businesses, the first day is going to be crazy," Mason explains.

Mission Minis, a San Francisco bakery that opened in January, was bombarded with 72,000 cupcake orders after a Groupon offer in March. Owner Brandon Arnovick says his frazzled bakers couldn't keep up, making some customers angry. Despite the chaos, he says the experience did have an upside: The shop has been baking as many as 1,700 cupcakes a day, vs. about 800 before the offer. Plus, the ordeal taught employees how to deal with disgruntled customers and work under pressure. "It was fun," he says. "Kind of."—*Joseph Galante*

The bottom line *Groupon's popularity could backfire if it doesn't help small business clients deal with customer surges from its promotions.*

Drawing Board



Biotechnology

Can Cloning Save The White Rhino?



▸ San Diego's Frozen Zoo stores cells of endangered species

▸ "It gives me hope we can help save species from extinction"

For a northern white rhinoceros, Angalifu has a pretty sweet life. The two-ton rhino can roam freely through a 213-acre habitat that resembles the African savannah. Still, Angalifu and his pal Nola, an elderly female at the zoo, are two of eight northern white rhinos believed to be left on the planet. "These beautiful animals are on the brink," says Oliver Ryder, the chief geneticist at the San Diego Zoo's Institute for Conservation Research. "There are a few left, but it's not clear they're capable of reproducing."

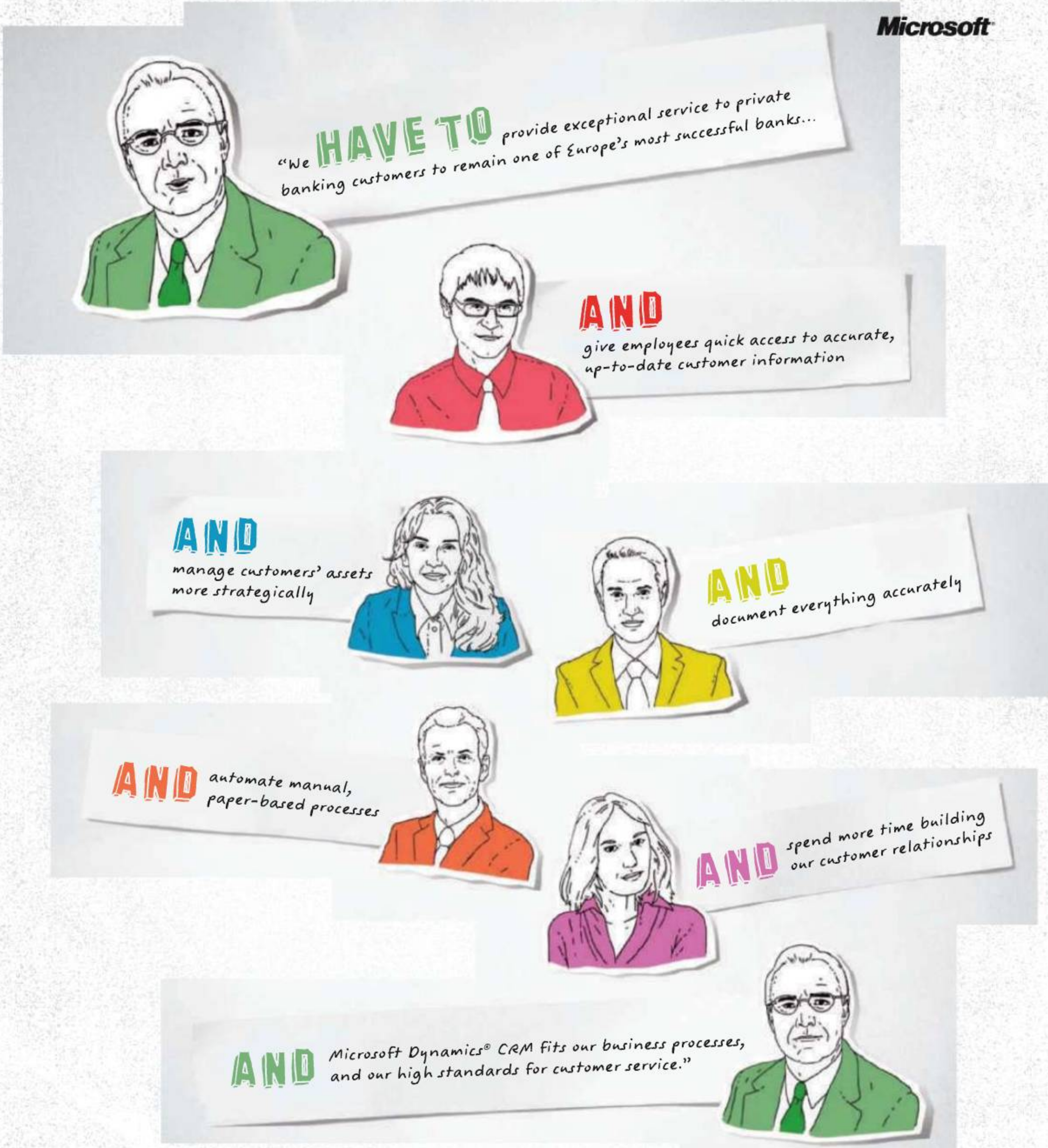
Ryder oversees the Frozen Zoo, a lab where skin cells and DNA from 12 white rhinos and 8,400 other animals–a total of some 800 species–are stored at -280F. The hope is that scientists can use the cells to create cloned animals and replenish endangered species.

The lab was founded in 1972, but technology needed to make use of the cells is just now being developed. This winter researchers at the Scripps Research Institute used tissue from the Frozen Zoo to create stem cells from the silver-maned drill, Africa's most endangered monkey. On June 1 the stem cells morphed into brain cells. "I thought, 'We've done it!'" says Jeanne Loring, who led the research. "It gives me hope we can help save species from extinction."

The next step will be to use the stem cells in some variation of the method used to clone Dolly the sheep. In 1996, Scottish scientists made Dolly by transferring the nucleus from an adult sheep cell into a developing egg cell that had its nucleus removed. They used

FROM TOP: KEN BOHN/SAN DIEGO ZOO/MINDEN PICTURES; ILLUSTRATION BY MIKE LUCKOVICH/ATLANTA-JOURNAL CONSTITUTION/CREATORS SYNDICATE

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embryonic stem cells in that process; Loring would use the stem cells she developed from the drill's skin since embryos from endangered animals are hard to come by. Loring and her team may also try mixing the drill cells with a three- to four-day-old embryo for a similar animal that's in plentiful supply, like a baboon. Offspring from this mix could be selectively mated to breed out the nondrill genes, in theory leaving a pure drill.

The cell-transformation technique, developed three years ago by Shinya Yamanaka of Japan's Kyoto University, uses a harmless virus to carry genes into skin cells—and change them into stem cells. Although the technique worked for the drill, it fell short when used with white rhino cells, so Loring is hoping to map the rhino's genome to get clues about which of its genes may reprogram cells.

Scientists have harvested stem cells from embryos for more than a decade, but Yamanaka's technology is important because embryos aren't always available for endangered species. Attempts to clone endangered animals, though, have led to aborted pregnancies and deformed offspring. In 2000, cells from the Frozen Zoo were used to clone two endangered types of cattle—a gaur and a banteng—using the Dolly method. Two of the three calves died shortly after birth. The surviving banteng lived at the San Diego Zoo for seven years, less than half its normal life span, and died in April.

Some scientists say those examples show the moral complexity of cloning. The benefit may be limited if only a handful of animals are created and live in zoos, says Autumn M. Fiester, a senior fellow at the Center for Bioethics at the University of Pennsylvania. "There has been a lot of suffering with these early deaths and malformations," Fiester says.

Ryder acknowledges the problems. "We would only engage in these efforts if there were no other way to prevent extinction," he says. For Ryder, the only rationale for cloning is to create new animals that could mate with existing ones, boosting their population and genetic diversity. With the white rhino, though, he and Loring are up against a deadline: Angalifu is pushing 40, and rhinos generally don't live past 50.
—Rob Waters

The bottom line *Clones made from skin cells may help revive endangered species, but some experts say cloning is the wrong solution to the problem.*

Innovator

Tod Dykstra



The Berkeley MBA is selling traffic-control technology that targets the most annoying drivers: those who clog streets in search of cheap parking

Tod Dykstra looks out from his downtown San Francisco office window every day and sees waste. While a parking garage next door sits empty, roads are clogged with cars in search of cheaper metered spots on the street. "Thirty percent of driving in cities is made up of people who have gotten where they want to go and are looking for parking," Dykstra says. "Think about all those carbon emissions. It just doesn't seem right."

Dykstra, founder of Streetline Networks, a San Francisco company that makes traffic-control technology, wants to make it tougher to park cheaply or get away with not feeding the meter. Streetline's system lets parking authorities identify crowded streets and jack up parking-meter rates block by block. The idea is to encourage drivers to stop circling and get off the streets—either paying for a municipal garage or heading to a less crowded neighborhood. San Francisco and Los Angeles are now installing Streetline technology.

Unlike anticongestion programs in London and Singapore, which rely on cameras and in-car devices called transponders to bill drivers as they enter crowded areas, Dykstra taps streets for data. Low-power magnetic sensors about the size of a palm are embedded in roads to detect cars in parking spots or driving. Those data are wirelessly transmitted to devices on top of streetlamps or traffic-signal boxes, which send the data to parking authorities. If a street has high traffic and no parking spots, San Francisco's SFpark agency plans to raise meter rates up to $6 an hour. The prices will show up on meters and the city's website.

The system also sends expired-meter data to smartphones carried by officers who can issue tickets. Each Streetline sensor costs $300 for installation plus a $120-per-year software license fee. San Francisco, where drivers feed meters only 55 percent of the time, says it's planning to buy 8,000 sensors. According to the city, an early test nailed so many scofflaws, the system paid for itself within two months. "The ultimate hammer will be the parking ticket," says Dykstra.

Streetline's technology grew out of a Pentagon-funded project Dykstra worked on while serving on the boards of Bay Area nonprofits focusing on environmental sustainment efforts. The research looked into sprinkling "smart dust"—millions of tiny sensors that measure temperature, pressure, sound, and other factors—over hundreds of square miles. Then a computer would gather the data and analyze it in real time. That project ended in 2001, and Dykstra, 48, founded Streetline four years later.

A self-described environmentalist who grew up in the Bay Area, Dykstra says he plans to sell sensors that monitor city water pipes for leaks. "Once you get things instrumented," he says, "you find you can do all sorts of interesting things to help save the planet." Ⓑ *—Cliff Edwards*

Battle cry ▶ "The ultimate hammer will be the parking ticket"
Background ▶ Worked on a Pentagon-funded "smart dust" project
Next up ▶ Systems to monitor lighting usage and water-pipe leakage

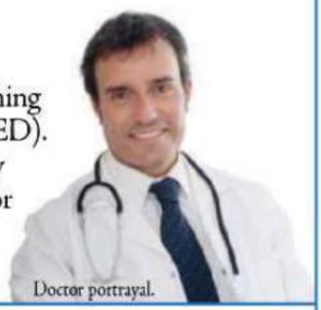
PHOTOGRAPH BY ROBYN TWOMEY FOR BLOOMBERG BUSINESSWEEK

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"I thought at my age there was nothing I could do about it, then I had 'the talk' with my doctor."

Your Doctor Talks to Men About ED Every Day



Doctor portrayal.

Your doctor will tell you that there is something you can do about your erectile dysfunction (ED). In fact, millions of men over 40 have already taken the first step and talked to their doctor about ED. And so can you.



Need Some Ideas on How to Open Up to Your Doctor?

The hardest part about having 'the talk' is getting those first few words out. Here are some ideas to help you break the ice when your doctor asks how everything's going:

The Direct Approach:
"I have trouble sometimes in bed. Could it be ED?"

The Indirect Approach:
"Is it true age affects sexual performance?"

The Silent Approach:
Just hand this ad to your doctor, he'll take it from there.

Running the Numbers

Did you know half of all guys over 40 have some form of ED? Here are some numbers to keep in mind from a recent survey of men with ED:



of men were anxious about talking to their doctor about ED.



of men felt relieved after talking to their doctor.



Tell Me More

To learn more about VIAGRA for the treatment of ED, and ED in general, visit **viagra.com** today. You'll find an online sexual health quiz, videos of guys with ED who've had the VIAGRA Talk and other helpful information.

Over 20 million men have already had their VIAGRA Talk. Isn't it time you had yours?

Important Safety Information

We know that no medicine is for everyone. Don't take VIAGRA if you take nitrates, often prescribed for chest pain, as this may cause a sudden unsafe drop in blood pressure.

Talk with your doctor first. Make sure your heart is healthy enough to have sex. If you have chest pain, nausea, or other discomforts during sex, seek medical help right away.

In the rare event of an erection lasting more than four hours, seek immediate medical help to avoid long-term injury.

In rare instances, men who take PDE5 inhibitors (oral erectile dysfunction medicines, including VIAGRA) reported a sudden decrease or loss of vision, or sudden decrease or loss of hearing. It is not possible to determine whether these events are related directly to these medicines or to other factors. If you experience any of these symptoms, stop taking PDE5 inhibitors, including VIAGRA, and call a doctor right away.

The most common side effects of VIAGRA are headache, facial flushing, and upset stomach. Less common are bluish or blurred vision, or being sensitive to light. These may occur for a brief time.

VIAGRA does not protect against sexually transmitted diseases including HIV.

Please see Important Facts for VIAGRA on the following page or visit viagra.com for full prescribing information.

For free information, including questions to ask your doctor, call 1-888-4VIAGRA (1-888-484-2472).

VIAGRA®
(sildenafil citrate) tablets

You are encouraged to report negative side effects of prescription drugs to the FDA. Visit www.FDA.gov/medwatch or call 1-800-FDA-1088.

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Pfizer

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IMPORTANT FACTS

VIAGRA® (vi-AG-rah)
(sildenafil citrate) tablets

IMPORTANT SAFETY INFORMATION ABOUT VIAGRA

Never take VIAGRA if you take any medicines with nitrates. This includes nitroglycerin. Your blood pressure could drop quickly. It could fall to an unsafe or life-threatening level.

ABOUT ERECTILE DYSFUNCTION (ED)

Erectile dysfunction means a man cannot get or keep an erection. Health problems, injury, or side effects of drugs may cause ED. The cause may not be known.

ABOUT VIAGRA

VIAGRA is used to treat ED in men. When you want to have sex, VIAGRA can help you get and keep an erection when you are sexually excited. You cannot get an erection just by taking the pill. Only your doctor can prescribe VIAGRA.

VIAGRA does not cure ED.

VIAGRA does not protect you or your partner from STDs (sexually transmitted diseases) or HIV. You will need to use a condom.

VIAGRA is not a hormone or an aphrodisiac.

WHO IS VIAGRA FOR?

Who should take VIAGRA?

Men who have ED and whose heart is healthy enough for sex.

Who should NOT take VIAGRA?

- If you ever take medicines with nitrates:
    - Medicines that treat chest pain (angina), such as nitroglycerin or isosorbide mononitrate or dinitrate
- If you use some street drugs, such as "poppers" (amyl nitrate or nitrite)
- If you are allergic to anything in the VIAGRA tablet

BEFORE YOU START VIAGRA

Tell your doctor if you have or ever had:

- Heart attack, abnormal heartbeats, or stroke
- Heart problems, such as heart failure, chest pain, or aortic valve narrowing
- Low or high blood pressure
- Severe vision loss
- An eye condition called retinitis pigmentosa
- Kidney or liver problems
- Blood problems, such as sickle cell anemia or leukemia
- A deformed penis, Peyronie's disease, or an erection that lasted more than 4 hours
- Stomach ulcers or any kind of bleeding problems

Tell your doctor about all your medicines. Include over-the-counter medicines, vitamins, and herbal products. Tell your doctor if you take or use:

- Medicines called alpha-blockers to treat high blood pressure or prostate problems. Your blood pressure could suddenly get too low. You could get dizzy or faint. Your doctor may start you on a lower dose of VIAGRA.
- Medicines called protease inhibitors for HIV. Your doctor may prescribe a 25 mg dose. Your doctor may limit VIAGRA to 25 mg in a 48-hour period.
- Other methods to cause erections. These include pills, injections, implants, or pumps.
- A medicine called REVATIO. VIAGRA should not be used with REVATIO as REVATIO contains sildenafil, the same medicine found in VIAGRA.

POSSIBLE SIDE EFFECTS OF VIAGRA

Side effects are mostly mild to moderate. They usually go away after a few hours. Some of these are more likely to happen with higher doses.

The most common side effects are:

- Headache • Feeling flushed • Upset stomach

Less common side effects are:

- Trouble telling blue and green apart or seeing a blue tinge on things
- Eyes being more sensitive to light • Blurred vision

Rarely, a small number of men taking VIAGRA have reported these serious events:

- Having an erection that lasts more than 4 hours. If the erection is not treated right away, long-term loss of potency could occur.
- Sudden decrease or loss of sight in one or both eyes. We do not know if these events are caused by VIAGRA and medicines like it or caused by other factors. They may be caused by conditions like high blood pressure or diabetes. If you have sudden vision changes, stop using VIAGRA and all medicines like it. Call your doctor right away.
- Sudden decrease or loss of hearing. We do not know if these events are caused by VIAGRA and medicines like it or caused by other factors. If you have sudden hearing changes, stop using VIAGRA and all medicines like it. Call your doctor right away.
- Heart attack, stroke, irregular heartbeats, and death. We do not know whether these events are caused by VIAGRA or caused by other factors. Most of these happened in men who already had heart problems.

If you have any of these problems, stop VIAGRA. Call your doctor right away.

HOW TO TAKE VIAGRA

Do:

- Take VIAGRA only the way your doctor tells you. VIAGRA comes in 25 mg, 50 mg, and 100 mg tablets. Your doctor will tell you how much to take.
- If you are over 65 or have serious liver or kidney problems, your doctor may start you at the lowest dose (25 mg).
- Take VIAGRA about 1 hour before you want to have sex. VIAGRA starts to work in about 30 minutes when you are sexually excited. VIAGRA lasts up to 4 hours.

Don't:

- Do not take VIAGRA more than once a day.
- Do not take more VIAGRA than your doctor tells you. If you think you need more VIAGRA, talk with your doctor.
- Do not start or stop any other medicines before checking with your doctor.

NEED MORE INFORMATION?

- This is only a summary of important information. Ask your doctor or pharmacist for complete product information OR
- Go to **www.viagra.com or call (888) 4-VIAGRA (484-2472).**

Uninsured? Need help paying for Pfizer medicine? Pfizer has programs that can help. Call **1-866-706-2400** or visit www.PfizerHelpfulAnswers.com.

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For Analysts, Things Are Always Looking Up



GETTY IMAGES

▶ **They're raising earnings estimates for U.S. companies at a record pace**

▶ **As a group, McKinsey says, they have been "persistently over-optimistic for 25 years"**

For years, the rap on Wall Street securities analysts was that they were shills, reflexively producing upbeat research on companies they cover to help their employers win investment banking business. The dynamic was well understood: Let my bank take your company public, or advise it on this acquisition, and–wink, wink–I will recommend your stock through thick or thin. After the Internet bubble burst, that was supposed to change. In April 2003 the Securities & Exchange Commission reached a settlement with 10 Wall Street firms in which they agreed, among other things, to separate research from investment banking.

Seven years on, Wall Street analysts remain a decidedly optimistic lot. Some economists look at the global economy and see troubles–the European debt crisis, persistently high unemployment worldwide, and housing woes in the U.S. Stock analysts as a group seem unfazed. Projected 2010 profit growth for companies in the Standard & Poor's 500-stock index has climbed seven percentage points this quarter, to 34 percent, data compiled by Bloomberg show. According to Sanford C. Bernstein, that's the fastest pace since 1980, when the Dow Jones industrial average was quoted in the hundreds and Nancy Reagan was getting ready to order new window treatments for the Oval Office.

Among the companies analysts expect to excel: Intel is projected to post an increase in net income of 142 percent this year. Caterpillar, a multinational that gets much of its revenue abroad, is expected to boost its net income by 47 percent this year. Analysts have also hiked their S&P 500 profit estimate for 2011 to $95.53 a share, up from $92.45 at the beginning of January, according to Bloomberg data. That would be a record, surpassing the previous high reached in 2007.

Despite the European debt crisis and high U.S. unemployment, the call is for profits to climb 34 percent

With such prospects, it's not surprising that more than half of S&P 500-listed stocks boast overall buy ratings. It is telling that the proportion has essentially held constant at both the market's October 2007 high and March 2009 low, bookends of a period that saw stocks fall by more than half. If the analysts are correct, the market would appear to be attractively priced right now. Using the $95.53 per share figure, the price-to-earnings ratio of the S&P 500 is a modest 11 as of June 9. If, howev-

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Learning from Wall Street's angriest bears page 48 ▶



er, analysts end up being too high by, say, 20 percent, the P/E would jump to almost 14.

If history is any guide, chances are good that the analysts are wrong. According to a recent McKinsey report by Marc Goedhart, Rishi Raj, and Abhishek Saxena, "Analysts have been persistently over-optimistic for 25 years," a stretch that saw them peg earnings growth at 10 percent to 12 percent a year when the actual number was ultimately 6 percent. "On average," the researchers note, "analysts' forecasts have been almost 100 percent too high," even after regulations were enacted to weed out conflicts and improve the rigor of their calculations. As the chart below shows, in most years analysts have been forced to lower their estimates after it became apparent they had set them too high.

While a few analysts, like Meredith Whitney (pages 43 and 48), have made their names on bearish calls, most are chronically bullish. Part of the problem is that despite all the reforms they remain too aligned with the companies they cover. "Analysts still need to get the bulk of their information from companies, which have an incentive to be over-optimistic," says Stephen Bainbridge, a professor at UCLA Law School who specializes in the securities industry. "Meanwhile, analysts don't want to threaten that ongoing access by being too negative." Bainbridge says that with the era of the overpaid, superstar analyst long over, today's job description calls for resisting the urge to be an iconoclast. "It's a matter of herd behavior," he says.

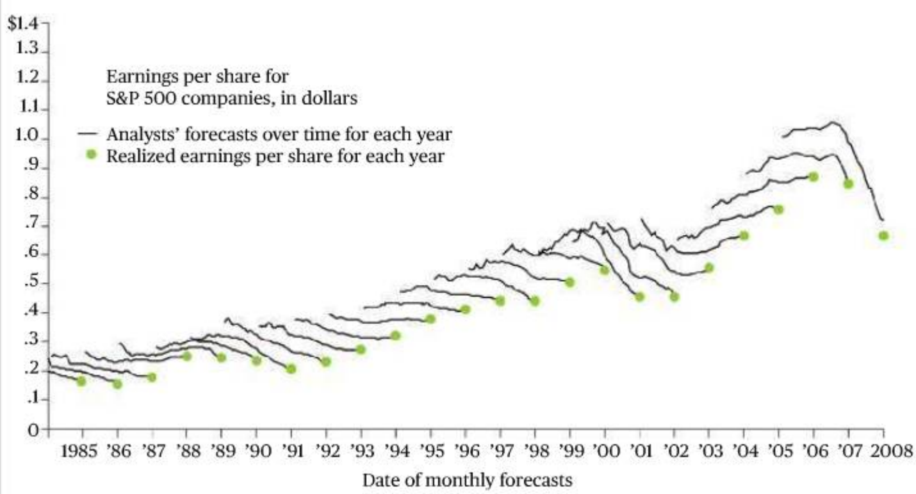
So what's a more plausible estimate of companies' earning power? Looking at factors including the strengthening dollar, which hurts exports, and higher corporate borrowing costs, David Rosenberg, chief economist at Toronto-based investment shop Gluskin Sheff + Associates, says "disappointment looms." Bernstein's Adam Parker says every 10 percent drop in the value of the euro knocks U.S. corporate earnings down by 2.5 percent to 3 percent. He sees the S&P 500 earning $86 a share next year.

As realities hit home, "It's only natural that analysts will have to revise down their views," says Todd Salamone, senior vice-president at Schaeffer's Investment Research. The market may be making its own downward adjustment, as the S&P 500 has already fallen 14 percent from its high in April. If precedent holds, analysts are bound to curb their enthusiasm belatedly, telling us next year what we really needed to know this year. —*Roben Farzad*

The bottom line *Despite reforms intended to improve Wall Street research, stock analysts seem to be promoting an overly rosy view of profit prospects.*

The Earnings Roller Coaster

Analysts have a long history of overestimating future profits. As this chart from McKinsey shows, analysts on average tend to start high and ratchet their numbers down as the companies get closer to releasing their results. Initial estimates proved to be too low in only a few cases.



DATA: THOMSON REUTERS I/B/E/S GLOBAL AGGREGATES; MCKINSEY ANALYSIS

Financial Regulation

How Banks Got Tripped Up By TruPS



▶ **Another financial innovation that got past the regulators**

▶ **"The industry was self-financing, using loopholes in rules"**

A battle has erupted in Washington over a seemingly obscure instrument called trust-preferred securities, or TruPS. This bit of financial exotica didn't get as much attention as synthetic collateralized debt obligations or credit default swaps during the global credit crisis. Yet TruPS definitely did some damage. Now Senator Susan Collins (R-Me., above) has proposed restricting them, and the banks are fighting back.

To understand what's at stake, consider the story of **Riverside National Bank of Florida**. Back when the industry was booming, Riverside sold at least $99 million of TruPS. The appeal for banks was that regulators counted the TruPS they issued as part of their capital—the buffer they are required to hold against potential losses. Riverside, based in Fort Pierce, Fla., was one of almost 1,400 U.S. lenders that had issued $149 billion of TruPS by the end of 2008, according to the Federal Reserve Bank of Philadelphia.

That by itself might not have become a problem. Securitization helped compound the dangers of these securities. Much as they did with mortgages, investment bankers pooled TruPS into CDOs, some pieces of which were sold to banks—including Riverside, which bought $211 million of them. When the real estate market soured and lenders racked up losses, Riverside and more than 400 of its peers suspended interest payments on their TruPS. That caused the CDOs holding TruPS to default or lose value,

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inflicting losses on the banks owning them. Thanks in part to those losses, Riverside, with assets of $3.4 billion, collapsed in April.

By issuing TruPS and buying CDOs containing them, the banks in effect were propping each other up. "The industry was self-financing, using loopholes in rules," says Joseph Mason, a professor of finance at Louisiana State University in Baton Rouge. "Regulators weren't keeping track of ownership of the capital, which became more difficult to do with the use of CDOs. The losses fed on each other."

The pileup of TruPS on banks' balance sheets went unnoticed by regulators since they were grouped with other investment-grade debt, according to three banking supervisors. Only last June were banks required to disclose their holdings of TruPS CDOs in regulatory filings. They still don't have to report purchases of TruPS that are not part of CDOs. "There wasn't enough oversight of the systemic risks that the banks' ownership of these securities could create," says Mark Williams, a former Fed examiner who teaches finance at Boston University.

TruPS may have their comeuppance in Congress. A provision that would prevent them from counting as Tier 1 capital was introduced by Senator Collins and included in the financial reform bill the Senate passed last month. The Senate version is being reconciled with the one the House of Representatives approved last month, which doesn't include a ban.

While Federal Deposit Insurance Corp. Chairman Sheila Bair supports the ban, banks are lobbying hard against it because it would force those that issued TruPS to raise capital in other ways. About 600 banks with less than $10 billion in assets use the securities as Tier 1 capital, says Camden Fine, president of the Independent Community Bankers of America, who wants the amendment to be withdrawn or at least to allow existing preferreds to continue counting as Tier 1 capital. "This is a raw-nerve issue with any banker that holds trust-preferred securities," Fine says. "I guarantee you every banker who holds [them] has contacted their representatives and senators on this issue."

OPPOSITE: COLLINS: ROLL CALL/GETTY IMAGES. THIS PAGE: DIMAS ARDIAN/BLOOMBERG

The Financial Life

Patrick Walujo



Walujo and his private equity firm have joined forces with TPG to troll for deals in Indonesia, one of the world's fastest-growing emerging markets

Lost amid all the scary headlines about debt crises in Greece and Hungary this year has been the spectacular performance of Indonesia. Southeast Asia's biggest economy grew 5.7 percent in the first quarter, and the vast archipelago has become the emerging market of choice for private equity pros. Patrick Walujo, 34, saw its potential as a resource-rich, fast-track economy years ago, and today is one of the country's premier dealmakers. Looking to invest in the Indonesia story, TPG Capital, the Fort Worth-based buyout firm, chose to team up with Walujo's private equity firm, Northstar Pacific Partners, back in 2006.

Since then, Northstar and TPG have done five deals worth a total of $1.3 billion. They include taking investment stakes in Jarkarta-based PT Bank Tabungan Pensiunan Nasional and PT Delta Dunia Makmur, the holding company of coal mining contractor PT Bukit Makmur Mandiri Utama. While rivals such as Washington-based Carlyle Group and the U.K.'s CVC Capital Partners are now getting serious about the world's most populous Islamic nation, Walujo is looking for ways to cash out of his first round of investments. "This year is going to be a year of a few exits," says Walujo, who graduated from Cornell University with a degree in industrial engineering. "Next year is going to be a busy year for exits."

TPG'S founding partner, David Bonderman, wants Walujo to keep trolling for fresh prospects, especially in the resource sector. (Indonesia is the world's biggest palm oil producer and has large deposits of natural gas and minerals such as coal and copper.) "Indonesia seemed to us to be an interesting emerging market for investment," says Bonderman, "and Patrick and his colleagues seemed to be the best there."

Walujo earned his dealmaking chops during stints with Goldman Sachs in New York and London. Bonderman likes his conservative investment style of avoiding fancy structured-debt deals for straight equity investments in companies that benefit directly from the country's expanding consumer base or natural resources. It doesn't hurt that Walujo is well-connected–he's the son-in-law of Theodore Rachmat, the former president-director of big automobile distributor PT Astra International and one of Indonesia's richest men. Walujo gets face time once a year with Indonesian President Susilo Bambang Yudhoyono.

Investing in Indonesia is still risky, what with the nation's corruption and weak legal system. Still, Indonesia is far more stable than when Walujo partnered with TPG in 2006. "We saw the opportunity in the private equity space in Indonesia," says Walujo. "At that time, there were not many people [who did]." Now Jakarta is brimming with dealmakers, and Walujo is leading the pack. B

—*Netty Ismail*

Company ▶ **Northstar Pacific Partners**

Strategy ▶ **Focus on companies benefiting from the Indonesian boom**

Big stakes ▶ **PT Bank Tabungan Pensiunan Nasional, PT Delta Dunia Makmur**

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Wall Street

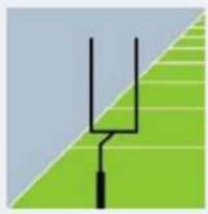
Goldman's 5-Terabyte Data Dump

The Financial Crisis Inquiry Commission says Goldman Sachs obstructed its investigation by delivering 5 terabytes, or 2.5 billion pages, of data in response to requests for information. Says FCIC Chairman Phil Angelides: "We did not ask them to pull up a dump truck to our offices and dump a bunch of rubbish." —*Ira Boudway and Caroline Winter*

5 terabytes, or 2.5 billion pages, would:



take **159** years to print out on a laser printer



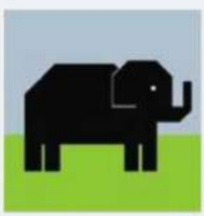
cover **28,700** football fields



fill **625** 8-gigabyte flash drives



make up **37.9 million** copies of *Bloomberg Businessweek*



weigh **12,500** tons, as much as 1,650 male elephants



equal the entire **Twitter archive** given to the Library of Congress in April

DATA: BRUCE NORDMAN, LAWRENCE BERKELEY NATIONAL LABORATORY; LIBRARY OF CONGRESS AND BLOOMBERG BUSINESSWEEK RESEARCH

Those voices have been heard. Senator Collins now says that lawmakers may have to grandfather existing TruPS or phase in the ban. The FDIC also supports grandfathering or allowing a transition period.

Even if the provision survives, it will come too late to undo the damage caused to Riverside. The bank has sued the firms that sold it CDOs for not disclosing that they were marketed to other lenders and sued the rating firms for overstating the creditworthiness of the securities. In a motion to dismiss the case, the investment banks denied that they made any misleading statements and said Riverside was a sophisticated institutional investor that should have done its homework. A separate motion to dismiss made by the rating firms said Riverside had failed to identify any statement that could be considered fraudulent. Both motions are pending.

One possible reason banks ended up owning so many TruPS CDOs: Investment bankers may have used relationships developed helping lenders issue TruPS to persuade them to buy related CDOs, says Joshua Rosner, an analyst at Graham Fisher, an independent research firm. "When [those bankers] didn't find enough natural demand among only institutional investors, they could turn around and sell back to the very banks that had issued into the last one, or would be selling into the next one," Rosner says. "It created a big Ponzi scheme." —*Yalman Onaran, Jody Shenn, and Alison Vekshin*

The bottom line *Securities designed to spread risk ended up magnifying losses in the banking industry when the economy slumped.*

Personal Investing

Top Stockpickers Come Up Short, Again

▶ **Eight of the 10 biggest U.S. mutual funds show lackluster results**

▶ **"It doesn't help if what you're selling isn't working"**

Only two of the nation's 10 biggest actively managed equity funds are beating their benchmarks this year, and both are from Fidelity. The fund company's Contrafund, with $63 billion in assets, gained 0.3 percent this year through June 3, edging out the Standard & Poor's 500-stock index by just over half a percentage point during that period, according to Bloomberg data. The $32 billion Fidelity Growth Company Fund rose 2.5 percent, beating its benchmark, the Russell 3000 Growth Index, by 2.6 percentage points.

The worst performer in the big 10 relative to its benchmark was the $37 billion Vanguard Windsor II, which fell 2.2 percent, trailing the Russell Value 1000 by 3.5 percentage points. The tepid showing of the most popular mutual funds comes after investors pulled $239 billion from domestic stock funds from 2007 through 2009, according to the Investment Company Institute. "It doesn't help if what you're selling isn't working," says James H. Lowell III, chief strategist at Adviser Investments in Watertown, Mass.

Over the past five years, an average of 44 percent of large-company U.S. stock funds have beaten their indexes, according to data from Morningstar. That poor showing has spurred investors to switch to lower-cost passive funds and exchange-traded funds, which track indexes rather than try to beat them. Morningstar figures show that in the 12 months ending Mar. 31, passive U.S. stock funds had inflows of $24.4 billion and



Danoff is keeping Contrafund ahead of the market

worldmags

Charlie Rose talks to

Meredith Whitney



Whitney, who runs her own investment advisory firm, is one of the bears profiled in this week's Cover Story. She's more downbeat about the market than she's been in a year.

What is the biggest factor in the market's current slide?
I think it is the disruption in Europe that's causing an overall de-risking. But the market's rise was really driven by expectations that earnings and unemployment would be far better than they've turned out to be. As we get into the second half of 2010, the hope for 2010 has diminished because the package of economic data has been disappointing. You've got challenges I don't think people fully thought through because they got market fatigue. For almost two years the market was going down. They wanted to be hopeful about something, and the fundamentals really didn't pull through for them.

Where would the U.S. economy be if we didn't have the debt problems in Europe and in Greece?
A lot the problems in our economy are our problems. For the last 30 years you've had a real structural shift towards a consumer-based economy driven by leverage. With or without Europe, you have the unavoidable issue of the consumer delevering. That means homeownership going from 70 percent probably back to 64 or 65 percent. You've had $1.5 trillion cut from credit-card lines. Europe is an important sidebar, but it's not the core reason the markets are still upset.

How do the next six months look?
I think there are massive structural problems underpinning the employment picture in the U.S. Small businesses, which employed about 50 million people and have been responsible for more than 60 percent of job creation over the last 15 years, have no way to fund themselves. So they're out of the game. You're left with the large corporate sector, which has shed only 3 million jobs. So it's mathematically impossible to get to a constructive job growth scenario.

Where is small business confidence today?
According to the latest survey that came out yesterday, it's improving. But when you ask small businesses what's the main reason why they are not hiring, they say lack of access to credit. Small businesses fund themselves through credit-card and home equity lines.

Are you optimistic about the next six months if small business gets access to money and unemployment begins to improve?
I don't believe there's going to be meaningful job creation, and I don't believe there's going to be a meaningful turnaround in spending. In fact, I am more bearish than I've been in a year. I have the strongest conviction that there's going to be a double dip in housing. I think you'll start to see that in July, August, September.

Wow.
Then the issue of the municipal market is one that's very scary to me because you have so many states with underfunded budgets—underfunded by two and a half times the level they were underfunded after the dot-com bust. That hurts the economy in terms of higher taxes, which squeeze the high end, and cutting programs and jobs, which squeeze the low end. People talk about the federal deficit all the time, but there's no timetable on the federal deficit that is as urgent as the state deficits because 49 states are constitutionally required to be balanced.

We've been reading these stories, you and I both, in *New York* magazine and other places, about the conflict between Wall Street—whatever that is—and the President. Does that have any impact on the market?
I think channeling all the blame to Wall Street has a massive impact. The politicians and government officials were easily as responsible for the real estate bubble as Wall Street was. So to place all the blame and put regulatory changes in place at a time of so much economic fragility weighs enormously on Wall Street. There was a senator who bragged about what he had done to stock prices the day after his amendment was adopted into the financial reform bill. I mean, an example is [Arkansas Senator Blanche] Lincoln winning the primary last night. She was failing in the primary race, and derivatives legislation was what got her so much attention. So everyone is piling on.

What sectors do you like?
There are companies within every sector that I like. I don't want to make too much of this comparison because it's not the Great Depression, but it's almost like a Joe Kennedy environment. He made all of his money during the Great Depression. If you have money, you can make a lot of money. And if you don't, it's going to be so much more expensive to be poor in this country. Ⓑ



Watch Charlie Rose on Bloomberg TV weeknights at 8 p.m. and 10 p.m.

OPPOSITE: ILLUSTRATION BY GREG MABLY; DANOFF: NATI HARNIK/AP PHOTO. THIS PAGE, FROM TOP: ROBYN TWOMEY/CORBIS OUTLINE; BRAD TRENT

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Big Funds, Small Returns

Most of the 10 biggest actively managed stock mutual funds are in the red this year.

Fund	Assets (billions)	2010 Return*
Growth Fund of America	$162.6	-2.41%
Investment Co. of America	62.7	-3.53
Fidelity Contrafund	62.8	0.30
Washington Mutual	50.9	-2.14
Fundamental Investors	47.6	-2.74
Dodge & Cox Stock	42.7	-0.75
Vanguard Windsor II	36.9	-2.15
Fidelity Growth	31.8	2.52
Davis New York Venture	30.9	-2.16
Vanguard Primecap	29.7	-3.20

*THROUGH JUNE 2 DATA: BLOOMBERG

stock ETFs drew $42.3 billion, while active U.S. stock funds had outflows of $27.6 billion.

Contrafund, managed by Will Danoff, is Fidelity's largest (excluding money-market funds). It invests in growth companies–those expected to increase earnings faster than competitors. It was boosted this year by gains in its biggest holding, **Apple**, which climbed 21 percent after the iPad's launch, and in **Berkshire Hathaway**, its third-biggest holding, which rose 5.8 percent. **Google**, the fund's No. 2 holding, has declined 20 percent. Contrafund has risen at an average annual pace of 4.3 percent over the past five years, beating 93 percent of similar funds, Bloomberg data show.

Apple is also the top holding at Fidelity Growth, run by Steven Wymer. The fund's second-biggest stake is in **salesforce.com**, the world's largest seller of Internet-based customer-management software; shares have advanced 22 percent this year. Over the past five years, the fund has climbed at an average annual rate of 5.1 percent.

Vanguard Windsor II, managed by six independent subadvisers, targets companies seen as undervalued when measured against earnings and other metrics. The fund has been hurt this year by its position in **BP**, which has dropped 34 percent since the Apr. 20 rig explosion. The fund had 1.5 percent of its assets in BP as of Mar. 31. "It's been a very volatile period of time, and you can be on the right side or the wrong side of that," says Dan Newhall, of Vanguard's portfolio review team. "And with volatility you can make some of your more compelling investments."

—*Sree Vidya Bhaktavatsalam and Christopher Condon*

The bottom line *With active managers failing to beat the market consistently, more investors are favoring index funds, which aim only to match the market.*

Real Estate

Home Bidding Wars Are Back in San Francisco

▶ The recovering tech industry and lack of supply boost prices

▶ "I wouldn't go nuts, but I would expect to see more improvement"

Hyuck Jae Lee and his wife, Seung Hye, vied with a dozen other suitors last month to buy a three-bedroom, 1,400-square-foot house in San Francisco's Inner Richmond neighborhood, a half block from Golden Gate Park. After having been outbid on a nearby home, the couple triumphed with an $875,000 offer, 14 percent above the asking price. "We feel like we're stepping into our San Francisco life," says Lee, a 38-year-old Silicon Valley engineer.

Four years after the housing bust began, at least one major market is hot again. Sales of houses and condominiums in the Bay Area jumped 50 percent in the first quarter from a year earlier and the median price rose 5.4 percent, to $685,000, according to a multiple listings analysis by Terradatum. San Francisco metro area values

Bloomberg Survey

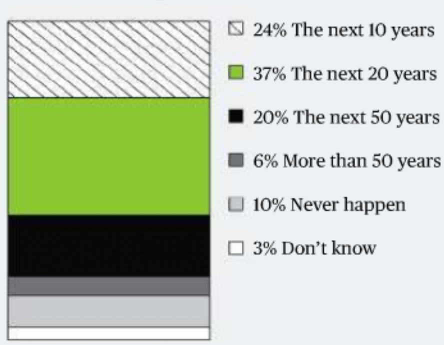
Market Professionals See Opportunity in the U.S.

Bloomberg conducts a quarterly survey of its customers. This poll is based on a random sample of 1,001 investors, traders, and analysts on six continents.

Which markets will offer investors the best and worst opportunities over the next year?*

	Best	Worst
U.S.	39%	9%
Brazil	29%	5%
China	28%	19%
India	27%	2%
European Union	12%	51%
Africa	7%	8%
Japan	7%	19%
Russia	6%	8%
Middle East	4%	15%
U.K.	4%	25%

How soon will China overtake the U.S. economy as the world's largest?



Which assets will offer the highest and the worst returns over the next year?

	Highest	Worst
Stocks	35%	17%
Commodities	23%	13%
Currencies	20%	6%
Bonds	11%	36%
Real Estate	7%	24%

65% Said the European debt crisis will slow U.S. growth modestly but recovery will continue

*UP TO TWO ANSWERS ACCEPTED. THE MARGIN OF ERROR IS PLUS OR MINUS 3.1 PERCENTAGE POINTS

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increased 16 percent in March from a year earlier, the biggest jump of any city in the S&P/Case-Shiller Home-Price Index. The 20-city composite measure climbed 2.3 percent.

"San Francisco has conditions of very restricted supply and lots of things that can push demand: an attractive climate, innovative economy, and high quality of life," says Harvard University economist Edward Glaeser, who has studied U.S. housing bubbles. In addition, the Bay Area's focus on technology and exports makes the region an early beneficiary of the U.S. recovery. A revitalized technology industry "almost certainly" drove the creation of 1,200 new jobs in the city from February through April, says Ted Egan, chief economist in the San Francisco controller's office. "I wouldn't go nuts, but I would expect to see more improvement."

Some factors may slow housing gains throughout the U.S., including the expiration of home-buyer tax credits and end of the Federal Reserve's purchase of mortgage bonds, says Robert Shiller, Yale University economist and co-creator of the home price index. Yet San Francisco's limited housing supply and global appeal help offset broader economic forces. "In supply-constrained and highly attractive markets there is no natural landing point for prices," says Glaeser. That helps explain why the San Francisco metropolitan area has ranked first or second among the most expensive U.S. housing markets for 19 of the past 20 years, according to data compiled by the National Association of Realtors.

Katherine Yung and Kevin Brandstetter understand that. They beat out 25 other bidders for a 1,600-square-foot house in the Golden Gate Heights neighborhood, offering $931,000, $162,000 over the asking price. The three-bedroom home has ocean views and an updated kitchen and borders on a small park. "Maybe we way overbid, but we came up with a number that was worth it for us," says Yung, who met her husband in medical school in St. Louis. "Now that we're in California, it's nice to see the ocean and the mountains."
—*Dan Levy*

The bottom line *San Francisco has unique attributes that help keep home prices high. With the tech sector recovering, buyers are willing to pay top dollar.*

FROM TOP: KEN MCKAY/REX USA; RICHARD B. LEVINE/NEWSCOM; KEITH KOSCAK, COURTESY RM AUCTIONS; CHRIS RATCLIFFE/BLOOMBERG

Bid & Ask

By Cristina Lindblad

Health Care

$3.9bn

Price that Grifols, Europe's largest maker of blood-plasma products, is paying for Talecris Biotherapeutics Holdings of North Carolina. Talecris has a big chunk of the $7 billion U.S. market for infused treatments for immune-system disorders. (Plasma, in case you don't have total recall of biology 101, is the watery yellow liquid that carries blood cells.)

Commodities

Crude for delivery in December 2018 traded at $92.78 a barrel on the New York Mercantile Exchange on June 4, vs. $71.51 for July 2010 delivery. The premium for delivery in eight years compared with the next-month price has shot up 86 percent since BP's Deepwater Horizon rig in the Gulf of Mexico exploded in April. The surge signals that the markets believe prices have nowhere to go but up as the biggest oil spill in U.S. history curbs drilling and makes it more expensive to develop new fields.

Fashion



A silk taffeta gown worn by Lady Diana Spencer in 1981 fetched the equivalent of **$275,000** at auction. The strapless, low-cut dress caused a sensation in Britain and helped turn Prince Charles' 19-year-old fiancée into a fashion icon. It was sold by its designers, Elizabeth and David Emanuel, and acquired by Chile's Museo de la Moda.



Beverages

$715mn

Price Coca-Cola is paying for the rights to distribute some of the brands of the Dr Pepper Snapple Group. The deal will allow Coca-Cola to sell Canada Dry and Dr Pepper, among other drinks, in some regions of the U.S. and Canada for 20 years. PepsiCo inked a similar **$900 million** agreement with the Texas-based company earlier this year.

Security

Marsh & McLennan is selling its Kroll security consulting operation to Altegrity for **$1.1 billion.** That's less than the $1.9 billion the insurance giant paid for Kroll in 2004. Altegrity, a private-equity-backed security firm that does everything from running background checks on U.S. government employees to consulting for foreign governments on military strategy, is led by Michael Cherkasky, who ran Kroll from 2001 to 2004.



Autos

A museum paid **$35,750** for the cab that whisked President John F. Kennedy's killer away from the scene of the crime, the Associated Press reported. Checker Motors donated the cab to the now defunct Pate Museum of Transportation in Texas in 1979. The Checker Marathon will henceforth be parked at Historic Auto Attractions in Illinois.

Insurance

$657mn

The cost to Prudential and its shareholders of the failed takeover of AIA—a figure roughly equivalent to one-third of the British insurer's 2009 operating profit. Prudential will pay AIA's parent, AIG, a breakup fee of **$223 million** for not completing the $35.5 billion transaction. The remainder is fees to lawyers and bankers who worked on the deal. Prudential Chief Executive Tidjane Thiam, who spent three months fighting to win investor support for the biggest acquisition in the firm's history, is now fighting for his job.

Energy

ABB, the Swiss company that is the world's largest supplier of power transmission equipment, offered **$1.3 billion** for Chloride Group, a British maker of gear to protect against outages. ABB's move sets up a potential bidding war for Chloride, which in April spurned a lower offer from Emerson of the U.S. ABB is on a shopping spree, having built up a **$7.2 billion** cash pile last year.

Banking

Countrywide Financial will pay **$108 million** to settle claims that it charged struggling homeowners excessive fees. Countrywide, once the top mortage servicer in the U.S. with a more than **$1.4 trillion** portfolio, was acquired by Bank of America in 2008.



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Michael Lewis

I Pledge to Write Funnier Columns



ILLUSTRATION BY TIMOTHY GOODMAN

Oath-taking is Wall Street's newest craze. Our columnist reveals the secret pledges of the new financial zealots

A few weeks ago Bloomberg News reported that, in just the past year, hundreds of students at the Harvard Business School have taken something called the MBA Oath. Endorsed by Harvard's dean and replicated by other business schools, the oath comes in two sizes: an important-sounding long version, and a punchy executive summary, consisting of seven crisp bullet points. (Sample bullet point: "I will refrain from corruption, unfair competition, or business practices harmful to society.") The gist of even the short version can be reduced further, to a single sentence: "Wherever I face a choice between my self-interest and the interests of the wider world, I pledge to act in the interests of the wider world."

News of the oath naturally aroused the interest of cynics everywhere and led them to raise hard questions: Isn't the underlying premise of free-market capitalism and the typical business school education that by doing well for oneself one is also doing well for the wider world? Is the typical business school graduate actually capable of seeing any difference between his own interest and the world's? Does this sort of mushy, vague-sounding oath serve society or the oath taker, who hopes that society will be duped into thinking that he is acting in its interests rather than his own? And anyway, if they are so keen to serve society instead of themselves, why do so many of these oath-takers wind up working on Wall Street, and, more specifically, for Goldman Sachs–whose CEO has been singled out by one of the oath's creators for blindness to the social consequences of his firm's actions?

Lost in this orgy of nay-saying was the mounting evidence that the MBA Oath already has had one clear practical consequence. In the past year graduates of Harvard Business School have flooded Wall Street, as graduates of Harvard Business School tend to do, and brought with them their new passion for oaths. It's too early to say if oath-taking has attained a permanent new high, or we are living through some kind of "oath bubble." What is clear is that many Wall Street firms, and Wall Street people, have found the need to have their own private oaths. In recent weeks several of these have leaked to *Bloomberg Businessweek*. We report them without further comment:

The Goldman Sachs Oath
We pledge not to call what we do "God's work," even though it is. We pledge to meet and even get to know ordinary people who do not work for Goldman Sachs so that we might better understand their irrational behavior and exploit it only when necessary. We pledge to create Wall Street's best-in-class oath.

The Morgan Stanley Oath
We pledge to stop trying to do whatever Goldman Sachs is doing. We, too, pledge to create Wall Street's best-in-class oath.

The Merrill Lynch Oath
We're just grateful to be asked if we have an oath. We do!

The Citigroup Oath
In our continued quest to make peace with the U.S. taxpayer, we pledge to sell our oath to the highest foreign bidder, the minute we decide what that oath should be.

The Oath of Hedge Fund Man
I pledge to short the credit spreads of only those public corporations and great nations that truly are doomed. I thus pledge to accelerate Darwinian forces that elevate the strong and destroy the weak. And even though that should be enough goodness for one lifetime, I pledge to bid generously for the sexier items at the next Robin Hood auction.

The Warren Buffett Oath
I pledge, even in the privacy of my own bedroom, to seem nothing like the above-mentioned hedge fund managers. I pledge to remain the go-to moral compass of the American money culture. To that end, I pledge to learn less than I typically do about the Wall Street businesses in which I invest, so that, after they are discovered to have lied, cheated, or stolen, I can plausibly claim to have known nothing about it. Specifically, I pledge to remain unable to find the headquarters of Moody's on a New York City map. (Really, I have no idea where the place is!)

The SEC Oath
We pledge to figure out who on Wall Street the American people most hate, and to sue them, even if we are sure to lose.

The Oath of the Financial Crisis Inquiry Commission
We pledge to find out, by the year 2050, what exactly happened on Wall Street in the early part of this century. We pledge to reform Wall Street. Or, failing that, to be taken seriously. Or, at a bare minimum, to attract a bit of media.

The Oath of the Federal Reserve
We pledge to regulate these oaths to prevent others from doing so. B

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PROFESSION: PILOT CAREER: ACTOR

People are acquainted with the star, the multi-faceted actor. But John Travolta is also a seasoned pilot with more than 5,000 flight hours under his belt, and is certified on eight different aircraft, including the Boeing 747-400 Jumbo Jet. He nurtures a passion for everything that embodies the authentic spirit of aviation. Like Breitling wrist instruments. Founded in 1884, Breitling has shared all the finest hours in aeronautical history. Its chronographs meet the highest standards of precision, sturdiness and functionality, and are all equipped with movements that are chronometer-certified by the COSC (Swiss Official Chronometer Testing Institute). One simply does not become an aviation supplier by chance.

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Time to Slip Into Something Less Comfortable?

The bearish forecasters who rose to fame in the market crash of 2008 have, for the most part, not surrendered their pessimism. Their moment could be coming back around.

By Jessica Silver-Greenberg

Photograph by Fredrik Broden
Illustrations by Barry Falls

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During the great credit party that raged around the world for the five years leading up to 2008, a few economists and investors studiously avoided the punch bowl. They stood in the corner, muttering darkly about how it would all end with the hangover of the century. They were outcasts. "I was lambasted and ridiculed as an idiot," says Michael Panzner, a stockbroker and author who began calling the collapse in 2005. "Like one of those guys holding a cardboard sign predicting apocalypse."

By the time Lehman Brothers collapsed and worldwide markets did their synchronized nosedive, Panzner had already published a book called *Financial Armageddon: Protect Your Future from Economic Collapse* and would soon follow up with *When Giants Fall: An Economic Roadmap for the End of the American Era.* Bearishness is a countercyclical asset; as the economy fell, the professional reputation of doomsayers soared. Suddenly they were the party animals. Gary Shilling, a veteran investment guru based in New Jersey, was feted for nailing all 13 of his investment guidelines for 2008, most of which involved shorting banks and housing. Banking analyst Meredith Whitney (page 43), who had shocked her peers with a devastating report on Citigroup when it was still widely viewed as fundamentally sound, started her own firm on the basis of her newfound celebrity. An obscure New York University professor named Nouriel Roubini, aka Dr. Doom, became a headliner on the international conference circuit, attracting actual groupies.

Then the ground started to shift. For most of the last year the U.S. economy has been inching toward recovery. While far from sunny, 2009 didn't bring with it much in the way of tent cities or snaking breadlines, as some of the most extreme bears said it surely would. The U.S. Labor Dept. reported that payrolls grew by 431,000 in May, marking the fifth consecutive month of gains. In April, sales at U.S. retailers edged up 8.8 percent from the same month last year. The major investment banks beat analysts' (admittedly depressed) earnings expectations, and the markets gained 80 percent in just over a year. Consumer confidence is up, and gross domestic product, though hardly robust, is growing at around 3 percent. Gradually the bears lost airtime, and most—although not Roubini—slipped from view.

Now, as the markets show fresh signs of panic, much of it emanating from the sovereign debt crisis in Europe, the spotlight is swinging back their way. Despite evidence of improving conditions, most bears have changed their outlooks only marginally, if at all. Which raises the question: Is their persistent pessimism a mark of brave, nonconformist thinking, or has their negativity become a kind of crisis schtick—contrariness for the sake of notoriety? To find out if they should be feared or ignored, *Bloomberg Businessweek* assembled a cast of the most prominent bears from 2008, traced the development of their dark outlooks, and assessed where they see the economy going from here.

"Zero interest rates are leading to an asset bubble globally... When you live in a bubble, everyone is delusional."
Nouriel Roubini, RGE Monitor



The Grizzlies

As early as 2004, Roubini, now 52, predicted an imminent recession caused by yawning U.S. trade deficits and a spike in oil prices and interest rates. It didn't come. In 2005 he again called for a recession. It didn't come. His revised prediction was for 2006. That year he spoke at an International Monetary Fund meeting and predicted the coming housing bust, saying the "United States was likely to face a once-in-a-lifetime housing bust... and ultimately a deep recession."

After Roubini's predictions finally came true and the world staggered into 2009, he said oil prices would remain low through the year, sinking to between \$30 and \$40 a barrel, and that the S&P would dip to 600. Neither happened. Oil jumped to \$70 a barrel in November and the S&P hit bottom at 676, then blew past 1000. Still, Roubini sees doom almost everywhere, including Brazil, one of the world's best-performing economies over the past year; he diagnosed it as at risk of "overheating" at an event last month in São Paulo.

Back in the U.S., where he recently celebrated the publication of *Crisis Economics: A Crash Course in the Future of Finance* with a lavish party hosted by Ken Griffin of Citadel Investment Group, he remains skeptical of the banks, as well as the debts run up by the federal government to resuscitate them. In a May 11 interview with Charlie Rose, Roubini pointed out that the government had picked up roughly \$40 billion of soured debt from now-deceased Bear Stearns

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and said "this buildup of public debt is something I worry about." He called the bailout of AIG "a mistake," and when prodded by Rose said that "zero interest rates are leading to an asset bubble globally." In the first chapter of *Crisis Economics,* Roubini argues that financial crises are predictable and not merely random events. In discussing this with Rose, he said: "When you live in a bubble, everyone is delusional." Present company excepted, naturally.

Roubini is the leading brand name in the community of market prognosticators who pride themselves on being outside the Wall Street Establishment. This independence, they say, allows them to see the fictions that people inside the system are blind to. Compared with the others, Roubini's forecast is mild. Most tend to view a double dip as a near certainty, with the second leg more brutal and destabilizing than the first.

One of the most famous of these extremist outsiders is Robert Prechter. In the 1970s he revived an old system of measuring investor psychology called the Elliott Wave Principle and used it to advise subscribers of his investment newsletter on Oct. 5, 1987, that they liquidate their stock holdings. Two weeks later, the market crashed. Prechter was hailed as a genius—though the label didn't stick. In 1993, *The Wall Street Journal* ran a page-one story headlined "Robert Prechter Sees His 3600 on the Dow—But 6 Years Late." He stayed pessimistic through the 1990s, and in 2002 said the Dow Jones industrial average would fall below 1000. It surged 25 percent the following year and kept going up until 2007.

According to Prechter, 61, the market's failure to crash as he predicted only set it up for more devastating blows down the road—which could be right now. Last March he correctly called the market bottom and predicted a rally. That has now run its course. The Standard & Poor's 500-stock index, he says, will dip below its March 2009 low. "From a peak in 2010, the stock market should fall for six years," he says.

"Government is acting like the last drunk at the party: Spending at an unprecedented rate, regulating the minutest areas of our lives, and strutting around as if it's solving problems."
Robert Prechter,
Elliott Wave International



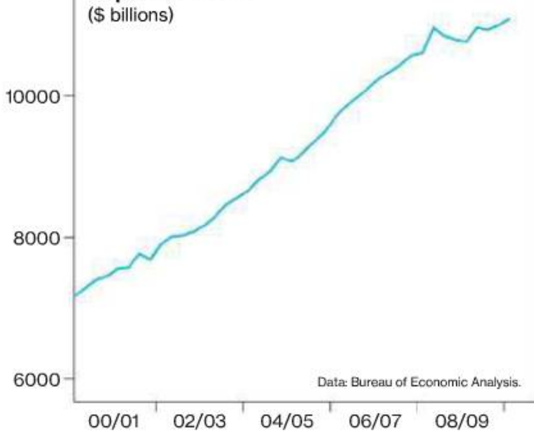
Although his pessimism remains the same, the basis of it has changed. This time around it's rooted in the actions of governments. "Government is acting like the last drunk at the party. Government is spending at an unprecedented rate, regulating the minutest areas of our lives, and strutting around as if it's solving problems as it creates them." Coming up next, according to Prechter? Another crisis in real estate and stocks. "The next crisis will encompass markets that are already off their highs: stocks, commodities, and real estate. But it will also extend to areas that have so far sailed through, namely corporate and municipal bonds, asset-backed bonds, and even many sovereign government bonds."

Money manager Peter Schiff was born an outsider—his father was a famous tax objector who is serving a lengthy sentence in an Indiana prison. Like Panzner, Schiff had a book on the shelves (*Crash Proof: How to Profit from the Coming Economic Collapse*) when the financial panic struck. His thesis, which revolved around the major structural flaws of the U.S. economy as well as what he saw as the inevitable collapse of the U.S. housing market, proved to be half correct. The second part of it, that investors could protect themselves by plowing their cash into foreign stocks, didn't pan out so well.

Schiff, 47, became a fixture on business television, fanning the flames with bold pronouncements that economic conditions were actually worse than people thought. Now he's attempting to leverage his notoriety into a run for the seat being vacated by Senator Chris Dodd (D-Conn.) Monetary policy, or what he sees as the colossal mismanagement of it by the Federal Reserve, is the centerpiece of his fledgling campaign. "Everything the government has done has been dead wrong," he says. "They have compounded the underlying problems in our economy."

On the campaign trail, Schiff gets worked up about the government's mishandling of the economy, especially the quasi-public mortgage agencies Fannie Mae and Freddie Mac that have consumed $125 billion in government

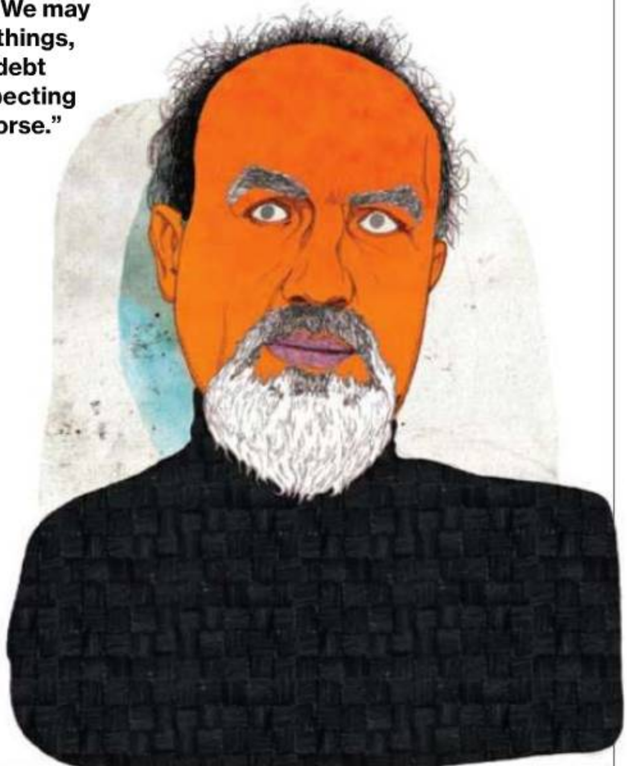
Disposable Income
($ billions)



Data: Bureau of Economic Analysis.

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"The same analysis I made in 2006 holds stronger today... We have a swelling of contingent liabilities and hidden risk. We may be cosmetically growing things, but our liabilities and our debt are growing, too. I am expecting that things will only get worse."
Nassim Taleb, author of *The Black Swan*



aid so far. According to Schiff, the Obama Administration's decision to save companies deemed too big to fail exacerbated the problems facing the country because it created an unmanageable federal deficit. "We bought some time, but the cost of the borrowed time is a great recession," he says. "Those who think otherwise were just fooled by phony economic growth produced by stimulus funds."

Schiff believes that frivolous personal spending has corrupted the U.S. economy and that it must be reformed by reconstituting the manufacturing sector. "We have to spend less and we have to invest more because there is going to be a depression that spans the Obama Presidency," he says, "and it has the potential to be really horrific." When asked about immigration, on the campaign trail—where he barely has made a dent against former World Wrestling Entertainment executive Linda McMahon in the Republican primary—Schiff answers that he's more worried about the opposite: "Ambitious, smart people are going to want to leave the country. No one is going to want to stay here."

Household Debt*
(as percent of disposable personal income)



Data: U.S. Federal Reserve.

Like Schiff, Panzner is an evangelist on the evils of debt, and finds confirmation of his views in the Moody's Investors Service statement in March that the U.S. government was at risk of losing its pristine AAA credit rating and might have to so drastically alter fiscal and monetary policy that it "will test social cohesion." Also like Schiff, he faults the government for not forcing Americans to reckon with the real consequences of the recession. "What makes this so much worse is that the government has been assuring people that everything will be O.K. and that a solution to this didn't require pain," he says. "That's just not true." Without a period of genuine austerity, he argues, the economy will never properly recover. "So yeah, I am a perma-bear," he says proudly. "Because none of the fundamental problems have been addressed, the government is still enabling companies to make risky loans, and even some of the same kinds of loans that helped contribute to the downturn in the first place."

Among the outsiders, Nassim Nicholas Taleb, 49, is the polemicist-in-chief. Famed for hectoring audiences of bankers (who invite him to speak and pay his five-figure speaker fees) and aggressively countering negative reviews of his work, Taleb gained a cult following when he published *Fooled by Randomness: The Hidden Role of Chance in the Markets and in Life* in 2001. It was, naturally, a screed that detailed how Wall Street deludes itself and investors with neat predictive models that regularly get blown apart by reality.

In 2002, Malcolm Gladwell profiled Taleb in *The New Yorker*, focusing on his investment in cheap, out-of-the-money options, betting that the market underestimated the likelihood of crashes. Then he shot to stardom with the publication of *The Black Swan: The Impact of the Highly Improbable* in May 2007, which extended his critique of risk management on Wall Street. Taleb argued that the models used to measure and contain risk were inherently flawed because they did not—and could not—take into account the existence of black swans, or unpredictable, potentially disastrous events.

Taleb's timing was exquisite: The book hit shelves just months before banks started announcing billion-dollar writedowns on their subprime holdings. *The Black Swan* hovered at the top of the *New York Times* best-seller list, was translated into more than 27 languages, and won Taleb an appointment as Distinguished Professor of Risk Engineering at New York University, a custom-fit title he's quite proud of. "It's the highest title that they bestow in the department," he says.

To Taleb's way of thinking, the worldwide response to the 2008 crash has only made the economy more vulnerable to black swans. "The same analysis I made in 2006 holds stronger today with even more force," he says. "It's worse on both

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"It's not about perception at all," says Gary Shilling of the need for consumer austerity. "I am a realist."

fronts. We have a swelling of contingent liabilities and hidden risk. We may be, cosmetically, growing things, but our liabilities and our debt are growing, too. I am expecting that things will only get worse because we wasted too much time not repairing the system. We are in an unprecedented time."

For pure bombast, Taleb's only rival is Marc Faber, who publishes the *Gloom, Doom and Boom Report* from his home in Hong Kong. Since 2002 the 64-year-old, Zurich-born economist has been predicting that the dollar would plummet in value, and since 2005 that an economic meltdown was about to hit the U.S. Faber now expects a sovereign-default domino effect, and he's not much rosier on China, saying in a Bloomberg Television interview that its economy might "crash" within the year. As for the S&P, he expects it to drop as much as 15 percent in the next six months. How will we cope with all this turmoil? In the June 2008 issue of *Gloom, Doom and Boom*, he recommended that Americans can help themselves by partaking in "prostitutes and beer" because they are "the only products still produced in the U.S."

Bears with Less Bite

When he last worked on Wall Street a quarter century ago, Gary Shilling, now 73, had a hard time being the bull his bosses wanted him to be. He believed the U.S. economy was in a long-term deflationary period and that bonds would prove to be a better bet than equities.

The last two years haven't shaken his certainty. He believes American consumers can't avoid a fundamental downshift in their spending habits. "It's not about perception at all," says Shilling, who was the chief economist at Merrill Lynch and has published an investment newsletter for the past 25 years. "I am a realist."

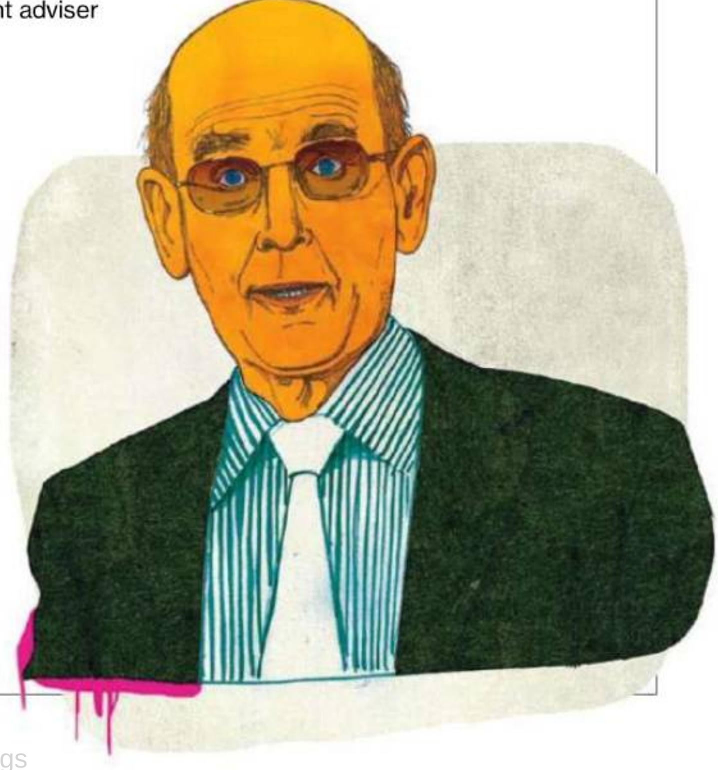
For someone who rejects the title of bear, Shilling has an unfortunate hobby: He keeps bees and frequently hands out jars of honey to friends—gifts far sweeter than his outlook on the global economy. After his stunning success in 2008, he kept investment advice unchanged heading into 2009, bluntly predicting "the worst global financial crisis and deepest world worldwide recession since the 1930s will continue throughout 2009," which *Business Insider* editors translated succinctly into "We are still screwed." He forecast a continued boom in U.S. Treasuries, as capital worldwide sought safety, and predicted that the S&P would end the year between 500 and 600 points. Not quite. It turned out to be almost double that, with Treasuries performing worse than the junk he warned investors away from.

Shilling holds to the view that recovery is a mirage whipped up by government stimulus, that the economy is held in check by declining home prices and contracting credit. Even though consumers had more personal income in March, according to the U.S. Commerce Dept., spending patterns didn't follow suit. The personal savings rate has been increasing, reaching 3.6 percent of disposable income in April. "With the decline of housing prices, consumers went off a cliff," he says. "They just don't have the kind of spending power or desire that they did in the past."

While many have focused on how the European debt crisis will effect U.S. trade with the Continent, Shilling sees it reigniting the banking crisis, which he contends has been papered over. "U.S. banks have $1.5 trillion in exposure to the euro zone and the U.K.," he says. "That's 48 percent of their total exposure, so the risk to the U.S. is predominately financial." Shilling doesn't mind one bit that 2009 returned him to the outskirts of popular opinion. Consensus around his views is bad for business. For his advice to be worthwhile to his newsletter subscribers, he says, "it's got to be something the herd doesn't see."

For Stephen Roach, traveling outside the pack is professionally precarious. Unlike most of the 2008 bears, he works within the financial Establishment, serving until recently as chairman of Morgan Stanley Asia. (He is now returning to New York, where he will split his time between Morgan Stanley and teaching at the Yale School of Management). "It's never easy, especially when you are working on Wall Street, especially when there is an awful lot at stake for the good times to continue," he says. "It's one thing to be

"With the decline of housing prices, consumers went off a cliff. They just don't have the kind of spending power or desire they did in the past."
Gary Shilling, investment adviser



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an academic who can make points purely for academic purposes. It's energizing to think and rethink your position."

Roach, 64, has been warning Wall Street of imminent pain since 2004, based on his conviction that runaway housing prices were feeding an unsustainable boom in consumer spending. When he moved to Hong Kong in 2007, he focused his consternation on the East, arguing that for the world economy to achieve stability, Asians would have to start spending more and American consumers would have to start saving more.

Although he concedes that "the world is definitely in better shape than it was a year and a half ago," he believes, like Shilling, that the European debt crisis will smack the U.S. hard. "No one wants to talk about the possibility of a double-dip recession," he says, "but it's very much there." The $962 billion aid package hammered together by the E.U. "is not going to be enough," he says. "Multiple contractions will inevitably follow." Monetary policy is a particular bugaboo for Roach because he believes that the preponderance of easy money led to the bubbles and bursts. "Fiscal and monetary policymakers haven't given me any confidence that they have adopted or even thought deeply about an exit strategy from zero interest rates and massive deficits."

Like Roach, Meredith Whitney made her dire predictions from within the financial Establishment, which is one reason they caused such a stir. As an analyst for Oppenheimer, Whitney, 40, put out a research report with the seemingly innocuous title, "Is Citigroup's Dividend Safe? Downgrading Stock Due to Capital Concerns." The conclusion, however, was jarring: Unless Citigroup raised $30 billion by chopping its dividend or quickly unloading assets, Whitney opined, it would surely fail. Citi's shares promptly swooned, and within days the bank's CEO, Chuck Prince, resigned.

Whitney left Oppenheimer and launched Meredith Whitney Advisory Group in February 2009, where she continued to predict trouble in the banking sector. The market judged otherwise. In the spring of 2009, as the banking sector rallied strongly off its historic lows, Whitney made no calls as unambiguously prescient as her Citi analysis. She was skeptical of the government efforts to revive the banks and maintained her bearish stance. She remains extremely cautious, contending that U.S. lenders face a tough second quarter because of rising capital requirements that will undercut their profitability.

"I am a skeptic who is trying to be less the prisoner of his own neurological makeup," says James Grant.

"A vast majority of last year's profits for the banks were government-induced," she told the Bloomberg Markets Global Hedge Fund & Investor Summit in May. "The government is putting a lifeguard on duty so that people will play in the pool." Still, she indicated that if prices fell further, she might dip a toe in the water and fish out some bank stocks. As for the housing market, "I'm steadfast in my belief that there's going to be a double dip," she says.

David Rosenberg, chief economist at Gluskin Sheff, has been as consistently bearish as Whitney, though he's less certain of a double dip. His is the cool, calm, and collected voice of doom, cautioning restraint and a dispassionate assessment of the markets. In his former job as chief North American economist at Merrill Lynch, Rosenberg was persistently wary of the boom surrounding him. In 2006 he circulated a research note called "Reassessing Hard Landing Risks" in which he argued that "you can't blindly look at a 4.7% unemployment rate and draw the conclusion that the labor market is tight enough to generate accelerating wage growth when there are as many as three potential job seekers out there for every available position."

As the subprime mortgage market contagion spread into 2008, Rosenberg estimated that the economy would barely notch any real growth, pegging his estimate at 1.6 percent. By the end of January, he'd already cut his forecast in half. He has long been more negative than most. In a 2008 Bloomberg survey of 55 forecasters, he ended up in the bottom 10 for his predictions on GDP, inflation, unemployment and the federal interest rate for 2006 to the middle half of 2008. Rosenberg has spent most of the past year casting doubt on the market rally, which he saw as a product of government

"A vast majority of last year's profits for the banks were government-induced. The government is putting a lifeguard on duty so that people will play in the pool."
Meredith Whitney, Meredith Whitney Advisory Group



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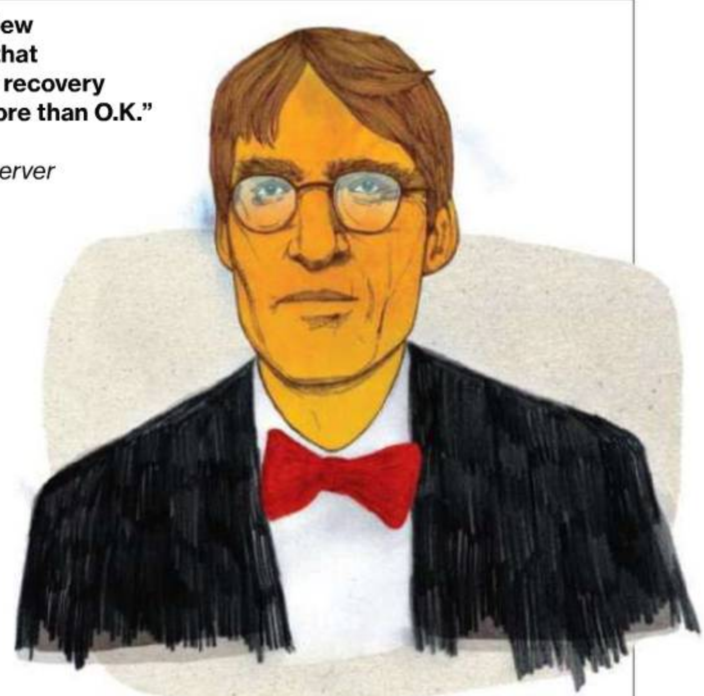
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stimulus and false hope. "Still no sign of organic private sector growth," he wrote on Feb. 3, 2010.

For now, he says, investors should understand that a "corrective phase is completely normal." The movement of the markets so far, he says, is pointing toward some "visible growth moderation toward the end of the year, but not a double dip recession." Rosenberg, 49, hasn't yet settled on the magnitude of the contraction. For now he's focused on the stability of whatever growth we've seen. "Mortgage applications for new purchases are down to levels we haven't seen since 1997 and there is a downdraft of jobs, so the recoveries are extremely fragile." But he allows that economic data don't tell the whole story. "The problem, of course, is essentially one of human emotion," he says. "We are essentially somewhere between Armageddon and Nirvana."

That's called a hedge.

"We did go forth with a view about nine months ago that the American economic recovery would be O.K. In fact, more than O.K."
James Grant, publisher,
Grant's Interest Rate Observer



The Domesticated

Even the most sophisticated people have difficulty switching world views, especially after their views have been affirmed. "Outlooks tend to be fairly deeply ingrained," says Julie K. Norem, an associate professor of psychology at Wellesley College. "Pessimists will pay attention to information that is punishing, not rewarding, and that's their fundamental outlook."

Some bears understand that—and are trying hard to change. Take Jeremy Grantham, the erudite 71-year old head of Grantham Mayo Van Otterloo, who trotted out his negative predictions to much public ridicule at the 2006 meeting of the IMF in Davos. While he has been predominately down on the economy since 1997, he has to balance his negative view of the economy against the demands of his day job, which is about making money for clients. During a January speech to investment advisers, he reflected on the price of his past bearishness: "We lost business like it was going out of style."

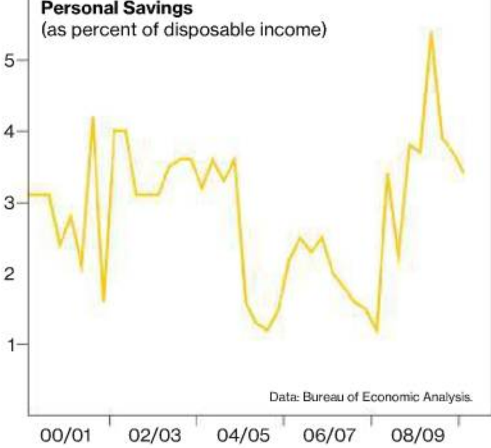
While he's certainly not a bull this time around, Grantham has taken a gentler tone on the U.S. economy's future. He says it won't be disastrous and is advising his clients to pick up stocks of U.S. companies with little debt and stable returns, which will beat out other large-cap firms. His latest newsletter, called *"Playing with Fire (A Possible Race to Old Highs),"* expresses both hostility to what he sees as the Federal Reserve's careless monetary policy and a flirty acknowledgment of the investment opportunities out there. Fed Chairman Ben Bernanke, Grantham writes, "is begging us to speculate."

James Grant, the 63-year-old publisher of *Grant's Interest Rate Observer*, also refuses to stick to pessimism merely for consistency's sake. Grant's reputation also soared in the 1987 crash—and fell during the two major bull markets since. *The Wall Street Journal* lampooned him in 1996 for being "a foolish idiot who was way behind the times," he says. "That's what I remember most about the errors of my impetuous youth, having an unshakable conviction that the credit difficulties were never really resolved, therefore the stock market was on shaky ground. It makes me very humble about what one can know about the future, and makes me less dogmatic."

Where not so long ago he saw inflated prices everywhere, he is now enthusiastic about undervalued assets, recently advising his newsletter clients to buy the despised stock of Yellow Pages publishers and steering them away from bonds ("bundles of promises to repay debt with valueless currency," he called them). The bookish investor, in jaunty pinstripes and tortoiseshell glasses, is actually optimistic about the economy—or at least optimistic for him. "I am a skeptic who is trying to be less the prisoner of his own neurological makeup," he says, before citing historical precedent: "There is a well-documented tendency for steep and ugly recessions to give rise not to weak and profitless recoveries, but to strong ones."

Peering out his office at a picture-perfect view of 300-year-old Trinity Church, Grant continued: "We observed this in the recessions of 1991 and 2001, which were meek and mild, and so were the corresponding recoveries." The deep recession of the early 1980s, on the other hand, led to a spectacular recovery. Based on that, Grant believes the rebound from this recession will be job-rich and strong, a position he has stuck to for nine months now. His bear suit has been sent out to the cleaners, and he doesn't know when it's coming back. **B**

Personal Savings
(as percent of disposable income)



Data: Bureau of Economic Analysis.

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Nine Questions (And Provisional Answers) About the Spill

Piercing the fog of the BP disaster, Peter Coy and Paul M. Barrett lay out the best current thinking

The sea is slow to reveal its secrets, and so is BP. The regulators and other companies caught up in the Gulf of Mexico oil disaster are almost as opaque. Whether motivated by the need for self-protection, the desire to get it right before releasing information, or the inevitable fog of a shape-shifting crisis, the sometimes conflicting statements released by BP, the Minerals Management Service, and others have left a raft of unanswered questions. How much oil is spewing into the Gulf each day? How much damage is it doing, and will the ecosystem ever recover? Who made the decisions that led to this nightmare?

The woman in charge of measuring the spill, Marcia McNutt of the U.S. Geological Survey, invoked the Rumsfeldian phrase "unknown unknowns" on May 27 while explaining why her Flow Rate Technical Group was having trouble figuring out how much oil was billowing from BP's broken well (more than 12,000 barrels a day, with no reliable upper limit). The same uncertainty surrounds enviromental impacts. "I don't think anyone knows, no matter what they say," says Nicholas Fisher, a professor of marine science at Stony Brook University in New York. "People want clean, simple answers to clean, simple questions, but we don't have them."

What follows is a careful attempt to take stock: asking the important questions and laying out the best current thinking on them. At the very least, we should all know what we don't know.

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Coated
A pelican is pulled from the waters off Queen Bess Island, La.

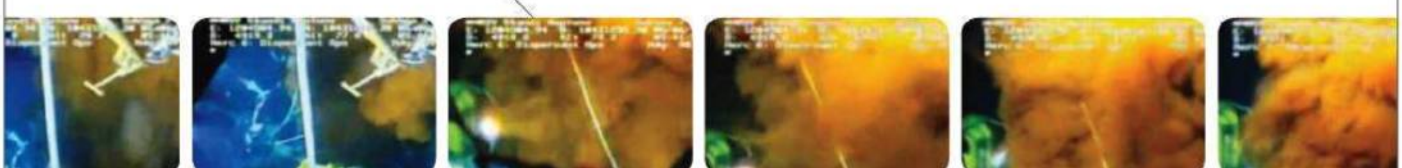
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Will part of the Gulf be a Dead Zone?

Big oil spills of the past are poor guides to the Deepwater Horizon disaster because all of them occurred in shallower water. This time, with the leak at 5,000 feet, a great deal of the oil hasn't reached the surface. Scientists say that under the immense pressure at that depth, much of it has turned into a diluted mist of hair-width droplets that are staying submerged in vast clouds. As recently as June 6, BP chief executive officer Tony Hayward said there was no evidence of such plumes in the Gulf. On June 8, however, the National Oceanic & Atmospheric Administration announced that they had indeed been found thousands of feet down.

Biologists have little experience with undersea plumes. "This is going to be groundbreaking science," says Roger Helm, chief of the environmental quality division of the U.S. Fish and Wildlife Service. Microbes that customarily feed on oil seeping from the seabed are expected to consume most of this oil, but that creates its own problems: The bugs use up oxygen needed by other sea creatures, potentially creating dead zones devoid of animal life, says Frank Muller-Karger, professor of biological oceanography at the University of South Florida. Marine biologist Rick Steiner says two-thirds of the fish and wildlife species injured in the Exxon Valdez spill 21 years ago have yet to fully recover. Stony Brook's Fisher says that the spill might promote bacteria that convert inorganic mercury into toxic methylmercury, which is taken up in the flesh of fish and other seafood.

Horror Show
Video feeds of the billowing oil



❷

Is there a chance the relief wells won't work?

Drilling two relief wells to stop the flow of oil is almost certain to get the job done, just not necessarily right away. "It's been done thousands of times," says Nansen Saleri, chief executive officer of Quantum Reservoir Impact in Houston. "Where the uncertainty lies is how much time it is going to take."

That's because it's fiendishly difficult to intercept the broken well, which is narrower across than a soccer ball, by drilling another well more than three miles beneath the ocean floor. Both relief wells might miss—as other emergency wells have—requiring a second, third, or fourth try, says Dave Rensink, president-elect of the American Association of Petroleum Geologists. It took Mexico's state-owned oil company, Petróleos Mexicanos, or Pemex, nine months to plug its Ixtoc I well after an explosion and fire in 1979. The company's first relief well failed, so it had to drill a second. Eventually more than 140 million gallons of crude spilled into the Gulf of Mexico.

Last year, a blowout at a rig off the Australian coast, owned by Thailand's national oil company, PTT Exploration & Production, required five attempts before it could be plugged by a relief well 10 weeks after the spill began. "Technology has improved, but it can take a while," energy banker Tudor Pickering Holt said June 7 in a note to investors. If the well is intercepted in August, as planned, stopping the flow may take another two weeks. BP must not only cement the well shaft but also plug the well bottom so oil and gas no longer flow into the hole.

OPPOSITE PAGE: MATTHEW HINTON/THE TIMES-PICAYUNE; THIS PAGE: TOP: A.J.SISCO/THE TIMES-PICAYUNE

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3

Will anyone go to prison?

Although outraged Americans would like to see people hauled off in handcuffs—for negligence, for obfuscation, or just as payback—the road from scorn to prison in cases of this kind is prohibitively long. Jail terms are "very rare," says Noah Hall, a law professor at Wayne State University in Detroit and former attorney with the National Wildlife Federation.

On June 1, U.S. Attorney General Eric Holder said the Justice Dept. had opened criminal and civil probes, although he didn't say which companies are being investigated. Holder said the government is looking into potential violations of the Clean Water Act and other environmental laws. Even if criminal charges are filed, such cases are typically settled with guilty pleas and the payment of fines. Hall says that prison terms, when they are imposed, are usually limited to cases of "spiteful, intentional acts," such as dumping a known toxic substance into a waterway.

Following the Exxon Valdez oil spill in Alaska in 1989, Exxon pled guilty to misdemeanors and was hit with $125 million in fines and restitution. (The ship's captain, Joseph Hazelwood, was convicted of a minor charge and did community service.) In the BP case, "based on everything public," Hall says, "I'm not sure we've seen enough that would warrant jail time."



Besieged
Obama is struggling to build a new coalition for environmental legislation in Congress

4

Is a climate and energy bill more or less likely to pass?

Here's a harsh political reality: The disaster that dramatizes the need to get America off oil makes it harder to pass a bill to help it do so. Before the spill, President Barack Obama tried to win Republican support for climate and energy legislation by tying it to expanded offshore drilling. That tactic is dead. Obama's new idea is to harness public anger and link a climate-and-energy bill to measures making offshore drilling safer. On June 2 he said the spill sends Congress an urgent signal to complete this work.

The House has already passed a climate bill; it's far from clear that the Senate's version will include a cap on carbon emissions—the most important and politically difficult provision. Also unclear is whether Obama will really fight for the cap, as he promised on May 26. Majority Leader Harry Reid has asked eight Senate committee chairmen to submit language for a new bill by the July 4 recess. The Senate's third-ranking Democrat, Chuck Schumer of New York, recently suggested that the Senate bill would omit the carbon cap, and that the sponsors of a climate bill, Massachusetts Democrat John Kerry and Connecticut independent Joseph Lieberman, could offer it as an amendment. Isolated in that manner, the cap would surely fail.

On June 8, Senator Lindsey Graham of South Carolina, the only Republican to help draft the Kerry-Lieberman bill, came out against it more forcefully than ever. The next day, he threw his support behind a weaker rival bill—one with no cap. Kevin Book, a managing director at ClearView Energy Partners, says Obama may need to win back Graham's support to get 60 votes for a filibuster-proof bill. For environmentalists, this is one crisis that may well go to waste.

FROM TOP: KLAUS TIEDGE/CORBIS; CHARLES DHARAPAK/AP PHOTO; OPPOSITE PAGE: MARK MOUTON

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5

Will oil reach the East Coast?

This may be the first big question with a definitive answer–and that is likely to be yes, according to a computer simulation released June 3 by the National Center for Atmospheric Research in Boulder, Colo. A detailed animation available on the center's website shows oil swirling slowly around the Gulf until it gets picked up by the Loop Current, a flow of warm water that snakes into the Gulf and then flows east. Scientists say the Loop Current could carry the slick at a speed of about 100 miles per day around the tip of Florida–potentially soiling the Keys, Biscayne Bay, and Miami Beach–and up the East Coast to the vicinity of Cape Hatteras, N.C. At that point, according to the computer simulation, most of the oil heads east toward the open ocean–some reaching across the Atlantic almost to the British Isles, home of BP. The simulation did not attempt to predict when that might occur.

Oddly, the planet might be better off if oil does escape to the Atlantic, where it will be diluted. The Boulder animation shows concentrations of oil close to the coasts of Florida, Georgia, and the Carolinas about 4 percent as dense as those near the wellhead, dropping to one ten-thousandth farther out in the ocean. Atlantic beachgoers won't like it, but the Loop Current could diminish the harm to the Gulf.

Ground Zero
Cleanup crews in Grand Isle, La., one of the first places touched by the spill

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On the Spot
Executives (left to right) from Transocean, BP, Halliburton, and Cameron

6

How did this happen—and who's to blame?

Investigators have begun to assemble the chain of errors that led to the disastrous Apr. 20 explosion that sank the Deepwater Horizon drilling rig, killing 11 crew members and causing oil to pour out of the ruptured riser pipe. What's not yet clear is who at BP and inside the federal government made the wrong decisions. The slide toward disaster was greased when BP sought and received permission to use pipes and casings in the well that deviated from the company's own policies. Then the company obtained an exemption to test the blowout preventer on top of the well at a lower pressure than federal rules required. BP pressed ahead even though, as e-mails released by House investigators show, employees had worried six weeks before the explosion that workers were struggling to control the well.

If the government had refused to bend its rules, or if BP had not sought exemptions in the first place, the Deepwater Horizon accident might not have occurred. What's unknown is whether the people who asked for and those who granted exemptions were defying orders or believed they were carrying out their superiors' wishes. Those questions are certain to be explored by investigators and plaintiffs' lawyers.

BP said it was recommitting to safety after a 2005 refinery explosion in Texas City, Tex., that killed 15, and a 2006 oil pipeline leak in Prudhoe Bay, Alaska It implemented a safety-oriented "operating management system" across 80 percent of company operations in 2009 and was rolling it out to the rest of the company this year. According to BP's annual sustainability review, the system "provides a single framework for all BP operations to follow, covering all areas from process safety, to personal health, to environmental performance." The unanswered question is why this brand-new system failed so utterly.



7

Could BP go bankrupt?

Estimates of the potential spill liability for all parties range into the tens of billions of dollars. Credit Suisse has said the disaster may cost BP alone as much as $37 billion over time, almost double this year's likely profit. That's raised questions about whether the British oil company will cut its dividend or put one or more of its units into bankruptcy proceedings to protect them from legal claimants and other creditors. The cost of BP credit default swaps soared on June 9, reaching nine times their pre-spill level.

Contrary to headline-grabbing predictions of doom, a Chapter 11 filing by BP seems unlikely, says Barry Adler, a bankruptcy expert at New York University Law School. "Despite the spill, this is a company with valuable assets and strong cash flow; it's hard to see BP reaching insolvency." Like many very large companies, BP is self-insured, meaning that it will pay claims out of its own pocket. "We are generating far and above the cash we need to satisfy all of the things we can see," BP CEO Tony Hayward said in early June.

If evidence of egregious wrongdoing surfaces, that could alter the bankruptcy outlook for BP. A civil jury assessing punitive damages or prosecutors seeking to make a point with enormous criminal fines could push the company toward insolvency. "The uncertainty of potential punitive damages or the credit risk that might come with serious criminal liability could change the picture," Adler notes.

Politics and public perception will also come into play. The Obama Administration could pressure BP into a reorganization, possibly via bankruptcy court, in which parts of the company were sold off and its leadership replaced. "If we get to the fall and the Loop Current has taken the oil around Florida, bankruptcy becomes a more viable option," says Burton LeBlanc of the plaintiff's law firm Baron & Budd.

FROM TOP: CAROLYN KASTER/AP PHOTO; D.HURST/ALAMY

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How will the oil spill lawsuits proceed?

It may take months, but the 200-and-counting leak-related lawsuits will be consolidated into one or more megacases–excruciatingly complex proceedings teeming with litigants and lawyers–and a single federal judge will emerge as the Solomon of the Spill. One man apparently angling for the job is U.S. District Judge Carl J. Barbier, a former head of the Louisiana plaintiffs' bar and thorn in the side of business. Barbier, who has been hearing preliminary legal motions, announced this month that he preemptively sold his oil-industry bonds to eliminate any "perception of a conflict in these cases."

Whoever ends up presiding over what may become one of the most convoluted courtoom struggles in U.S. history will wield extraordinary authority. Many plaintiffs' lawyers want to do battle in New Orleans, where Barbier sits; corporate defendants prefer Houston, U.S. headquarters of the oil industry. A federal panel in remote Boise, Idaho, will make the geographic call in late July.

Six of the 12 federal trial judges in New Orleans have recused themselves because of oil-industry investments or other connections to the controversy. Not Barbier, who was appointed by President Bill Clinton in 1998. "We think Judge Barbier would be a fine judge to preside over this unprecedented litigation," says Baron & Budd's LeBlanc. The Louisiana Association of Business & Industry would be "skeptical" of such a selection, says vice-president Ginger Sawyer. Her group opposed Barbier's appointment to the bench, noting his lobbying against legislation aimed at restricting civil lawsuits. In 2002, the U.S. Supreme Court vindicated the judge's refusal to step down from a tobacco-liability case, despite the cigarette industry's allegation of bias. The justices said he had no conflict.



Marked Man?
Hayward has his board's confidence, but pressure to oust him is building

9

Can BP CEO Tony Hayward last?

On June 7, some of the most powerful men in Britain–including Vittorio Colao, chief executive of telecom giant Vodafone; Martin Sorrell, head of the advertising conglomerate WPP; and John Sawers, chief of the British intelligence agency MI6–gathered at BP's London headquarters to show support for Tony Hayward. "We have learned that he is made of steel," said Chairman Carl-Henric Svanberg.

A show of support from VIPs not connected to the company won't protect Hayward, 53, forever. Yes, he's tough and energetic. Also, there is less anger over the spill in Britain. Nevertheless, says Gudmund Halle Isfeldt, an analyst at DnB NOR ASA in Oslo, "both Tony Hayward and the chairman are likely to go." Hayward's penchant for unfortunate turns of phrase–"I'd like my life back," for example–hasn't helped.

Andy Inglis, 50, the exploration and production head, had been considered Hayward's likely successor, except the calamity occurred in his unit. Refining and marketing chief Iain Conn, 47, has made a start at improving performance at BP's troubled refining and marketing operations and is respected by the board. Robert Dudley, 54, formerly headed BP's Russian affiliate TNK-BP but left it in 2008 during a battle with the company's Russian partners. On June 5, Hayward put Dudley, an American, in charge of a unit responsible for the cleanup. "If he does a great job at running the unit, there's no reason he can't go to the top," says Dougie Youngson, an analyst at Arbuthnot Securities in London. A potential outside candidate is Frank Chapman, 56, head of gas giant BG Group. Whoever takes over will have history's biggest image-rebuilding mission on his hands.

—With Stanley Reed, Margaret Cronin Fisk, Jim Efstathiou Jr., Pat Wechsler, Brian Swint, Jessica Resnick-Ault, David Wethe, and Justin Blum

FROM TOP: JOE BURNS/ALAMY; PAT SULLIVAN/AP PHOTO

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The Man Behind The Bandz

Robert Croak went from promoting concerts in east Toledo to the center of one of the hottest kiddie crazes in years. Here's how he did it

By Susan Berfield. Photographs by Michael Edwards

The UPS truck rumbles down Main Street in Toledo most mornings, past the boarded-up Cloud 9 bar, the abandoned Masonic Temple, the car wash, the tattoo parlor, and the payday loan shop. It stops at the small warehouse of BCP Imports (Brainchild Products), where a dozen young men, recently hired and plenty eager, rush to unload, sort, and repackage hundreds of boxes of Silly Bandz. They are this year's kiddie rage–brightly colored silicone bands shaped like the outlines of animals, letters, princesses, and more. Kids, and a few notable parents such as Sarah Jessica Parker, stretch them out to wear like bracelets. When taken off they revert to their original shapes. Kids also trade them, count them, and fling them, which is why they've been banned in some schools around the country. A pack of 24 costs about $5. Robert J. Croak, the 47-year-old founder of BCP, says he has sold millions.

Croak is sitting behind a desk covered with piles of paper and four computer screens, halfway through a bottle of chocolate Yoo-hoo. He's wound up and blustery, his voice raspy from late nights in the office. Croak has been a bar owner and concert promoter in Toledo's gritty east side for years. He grew up in the neighborhood, earned a degree in marketing from Owens Community College, then took over his grandmother's

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"[No one] has a reason to be happier than I am," says Croak

Main Street restaurant after she died and turned it into a rock club called Frankie's Inner-City lounge. For the past several years he has been selling custom t-shirts, dog tags, mugs, and silicone bracelets made popular by Lance Armstrong. Nothing in his background suggested that he would find himself at the center of one of the biggest successes in modern-day toy selling; Croak is an opportunist who has found the greatest opportunity of his life. "I'm the luckiest guy alive right now. I don't think you're going to find anyone who has a reason to be happier than I am," he says. "I have the hottest toy, the hottest fashion product on earth. All the right people like Silly Bandz. Everyone asks who my publicist is. I don't have one. We don't advertise. All we do is viral marketing. This is happening on its own."

$4.95

Suggested retail price for a pack of Silly Bandz

It might also end on its own, its energy exhausted, once kids' attention turns elsewhere. "This isn't a cultural phenomenon, it's a schoolyard fad," says Christopher Byrne, an independent toy consultant. "It's tracking the way a lot of fads do. The product is out there for awhile, it hits critical mass, then kids get tired of it." On the fad hierarchy, Silly Bandz might have reached the level of Kooky Klickers and scented erasers, but it has a long way to go before achieving the status of Beanie Babies. The products are also easier than most to copy–already, cheaper-looking imitations are widely available. Croak says he's not concerned about any of this, although he is trying to establish Silly Bandz as a brand that resonates beyond the bands themselves; after all, they have no logos, no characters, no stories. "We've been planning some new products that will make Silly Bandz a household name for the next 5 to 10 years," he says. As with many aspects of his company, he declines to get into specifics. "I'd love to share some details, but I can't."

About three years ago, Croak and the manager of the factory that produces his silicone bracelets visited a trade show in China, where the manager spotted stretchy animal shapes that were sold in Japan as rubber bands. "I liked the way they looked, and I thought if they were done correctly–larger and thicker–they would make a great fashion accessory," says Croak. "It's like any entrepreneur: If you see something you like and have the capability to develop it differently, then the sky's the limit. You know the Dyson vacuum guy who says in his

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Roughly 1,500 orders go out each day from BCP's warehouse

commercial that he had 180 prototypes before he got it right? With Silly Bandz, we got it right the first time."

The animal bands were hardly new. The Japanese creators had been recognized with a national design award and had been selling them in America in a limited capacity since 2002. The Museum of Modern Art Design Store carried them, as did the Japanese department store Takashimaya. *New York* magazine singled the animal bands out in October of that year, noting that they could be worn as bracelets. But what Croak saw in China "wasn't Silly Bandz," he says. "We trademarked the name. We created them. We created the craze."

Croak saw potential in the bands that the original designers didn't: If they were offered in a greater variety, kids might want to collect and trade them like Pokémon cards. It could be a $100 purchase made $4.95 at a time. Slowly and unpredictably, Silly Bandz began to draw kids in with its website, which Croak launched late in the summer of 2008. He also took full advantage of the new social order in promoting his product. The Silly Bandz Facebook page now has nearly 255,000 fans, and on YouTube, some 2,000 videos have been posted about the bracelets, including a rap song that has been played almost 24,000 times. "Silly Bandz are a great toy, a fashion accessory. There doesn't need to be a reason," Croak says when asked about the way his product took hold. "Why take the fun out of it?"

BCP is a private company, so sales figures aren't available. The bands clearly are a financial bonanza, however. Sean McGowan, a toy industry analyst at Needham & Co., estimates that a package of 24 bands probably costs nickels to produce at BCP's factory in China. Even after including packaging and transportation expenses, the profit margin could be close to 75%. As for Croak's marketing strategy, he prefers to keep the details secret, lest he surrender another profit opportunity: "I'll save that for a book deal, O.K.?" he says.

BCP went from obscurity to the *CBS Evening News* in a matter of months, and the pressure on Croak is intense. "It's chaos every day," he says. Still, he tries to maintain a relaxed office atmosphere: Music is constantly playing, and the dress code is casual—Croak wears jeans and untucked shirts, and many of his young employees are in shorts. Competition emerged months after Croak launched Silly Bandz. An entrepreneur named James Howard introduced Zanybandz in Birmingham, Ala., after testing the product out on his nieces. It could be that Silly Bandz and its competitor are actually helping one another: The greater the awareness of the product, the more sales for everybody. "Very often a second company ignites the whole market," says McGowan. Kids and stores don't necessarily care which brand they have. The bands spread to Tennessee, Florida, New Jersey, Connecticut. By the summer of 2009, "it started to get crazy," says Croak. "We thought we were ramping up enough then, and we've grown four times since then. It's a learning curve every week." Croak says BCP has gone from shipping 20 boxes of Silly Bandz a day to about 1,500. (The boxes contain anywhere from 24 to 500 packs.) He says Silly Bandz are carried in approximately 18,000 stores in 25 states.

75%

Estimated profit margin that Croak earns on every band sold

Croak's career hasn't been without its challenges. In 2002 he was convicted of one count of forgery for signing a check for a business associate and was put on probation. Two years later he was ordered to pay back taxes and penalties of about $45,000. "It was a technical violation of the law," he says, referring to the forgery. One of the terms of his probation was that he was no longer allowed to own or operate a bar. "As a result of this," he says, "I chose to pursue bigger and better things." Regarding his tax bill, he says: "Sometimes taxes don't get paid on time, there are economic reasons. All of my taxes are paid and current." Croak was also involved in a controversial city-run project to develop a Toledo Civic Theater for which he would book concerts. The first ones, in the summer and fall of 2008, were successful. After that, though, Croak ended his role amid fighting between the city council and the mayor over how contracts had been awarded. Croak's recent turn of fortune has been duly noted in east Toledo. Dan Steingraber, the chairman of a local business organization and a longtime associate, says: "It's fantastic. You never know what's going to make you money. Rob has been throwing s--- at the wall for a long time. It's good when something sticks."

These days, Croak is creating jobs in a place that's desperate for them. Once dominated by auto manufacturing, the Rust Belt city of roughly 300,000 now has an unemployment rate of 12%. Croak's office staff has grown from around 20 people to nearly 70 in the past year, and there are approximately 200 salespeople working around the country. (BCP's factory in China—Croak won't say where it is—also brought in 700 new workers in the past five weeks.) With the momentum continuing to build, Croak is recruiting people through Craigslist to take phone orders, maintain the Silly Bandz website, and deal with shipping to homes, toy stores, and, soon,

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Croak's Toledo-based workforce has grown from 20 to 70 in the past year

Macy's. After the local newspaper, *The Blade*, ran a story about Silly Bandz, so many people came to the office looking for jobs that Croak had to lock the doors. One night, behind on a deadline, he put up a post on Facebook and 20 people arrived to help within an hour. Jared Hissem, 28 and married with a young child to support, was holding down two jobs, doing data entry at a market research firm, and working behind the counter at KFC when he saw one of BCP's postings. A couple of days later he had quit his other jobs and was taking orders over the phone for Croak. "I had never heard of Silly Bandz until I got hired here. Now I love them," Hissem says. "And it's a laid-back work environment, with the music and all. I haven't left once in a bad mood." Another new member of the workforce, a 23-year-old college graduate named Marcus Ahle, started as a Web programmer in mid-May after searching for work for months. "I'm not worried about the fad ending," he says. "I'm just thankful to have a job in this economy." Until recently, Croak's workers were bringing hundreds of boxes of Silly Bandz a day to the post office to be weighed and stamped. The postmaster just asked Croak to get his own metering machine. He's not sure if he can keep up: "The demand changes every day. Supply-and-demand issues are good, though. It builds the anticipation and hype. A little scarcity is good."

Just 40 minutes into an interview in his cramped office, Croak starts to look anxious; he wants to see how things are going in the warehouse. "We have huge deals that are going to be national news," he says, "but I can't share them now. They're reaching out to us. We're reactive, not proactive." Although Walt Disney has signed up with a competing brand, Character Bandz/Forever Collectibles, there are plenty of other licensing possibilities for Silly Bandz, from the Simpsons characters to Dora the Explorer. "Let's just say that the best names and icons in the United States will be represented by Silly Bandz in the coming weeks," Croak says. He has just introduced a UV-activated beach pack that changes color when the temperature rises. And he lets on that he's going to put out his first celebrity pack, with a basketball player he won't name, as well as backpacks and notebooks for the new school year. He says he has been talking to the owner of an amusement park and to the YouTube rapper.

Croak envisions an empire of Silly Bandz, but if that doesn't quite come to pass, he says he'll be fine with it. "This is proof that the American dream is still alive. Beanie Babies are not the must-haves anymore, but people still buy them. If Silly Bandz turns into that, it's a great place to be." B

From One Fad Man to Another

Kyle Aguilar, CEO of Wham-O, the company behind the Frisbee, Slip 'n Slide, Hacky Sack, and SuperBall offers advice on long-term survival

Describe the life span of a hot toy.
It can last decades or just a season. Sometimes a product has its wave and then comes back. Last year a picture was snapped of the President's wife using a Hula Hoop. We've always had a hoop for exercise, but it became a big trend. We have to make sure we fill the demand when the trend hits. This will probably last about six months to a year. Then the big excitement will be over.

How do you fend off imitators?
People knock off our products on a continual basis because they sell. Take the Frisbee line. If we only focused on making a $5 or $10 Frisbee, then competition would come in with a $1 Frisbee. I make sure we're in all the price points so it leaves no room for our competition to bid against us.

What happens when a product goes cold?
It doesn't necessarily disappear. Before you were making 1 million a month, now you're making 10,000 a month. What you should do is build your brand off of that. When we made a new toy, at the end of the commercial, in a big strong voice, we'd say "made by Wham-O!"

What is your best-selling product of all time?
The Frisbee. It never loses its popularity. The Slip 'n Slide also still sells like crazy. Parents want a toy that holds the attention of a child for at least 15 or 20 minutes. The nostalgic toys we have never die off.

Any words of wisdom for the makers of Silly Bandz?
They've already built a brand for themselves, but I can see in the next few months that it's going to start to die off. They can sell to a bigger toy company, or they can take the profits and build a solid development and creative team and start to explore what the next great trend will be. They need to be ahead of the market.

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The Killer iPhone. How Apple designed its new model to be sweet to customers and vicious to rivals

Given how much was known about the fourth-generation iPhone before its official unveiling on June 7, Apple CEO Steve Jobs did quite a job to generate as much as excitement as he did. Fans and analysts raved over the $199 phone's videoconferencing feature, applauded its slimmed-down design, and looked forward to a promised new era of hyper-multitasking. The new iPhone is built not just to compete with other phones but to keep pushing the boundaries of the Apple universe. It's Apple at its most creative—and its most aggressive, as it attempts to divert revenue from advertisers, book publishers, and content providers.

By Cliff Edwards and Arik Hesseldahl

DATA: APPLE, IDC, PINCH MEDIA



Retina Display: The threshold at which the human eye can no longer tell whether one screen is better than another is about 300 pixels per square inch. Apple exceeds that with 326 pixels. Although displays found on other phones are bigger—Sprint's EVO 4G tops it by almost a full inch—it's the highest resolution ever used in a wireless phone, says iSuppli display analyst Vinita Jakhanwal. Apple is going for the last word on display quality and challenging others to match it. Look for Apple's rivals to respond with a display-resolution arms race before the year is out.

x 2

Cameras: While other phonemakers have gone megapixel-mad—Nokia, Samsung, and others boast cameras in the 8 to 12 range—Apple has held steady at five megapixels. A smart move, says Van Baker, analyst at Gartner who praises Apple's decision to instead increase the overall size of the camera sensor, which will do more for picture quality than adding megapixels. Additionally, iPhone 4 has a front-facing camera that's central to its marquee feature: Video calling. While technically not new—Nokia has offered it since 2007—Apple's version, FaceTime, is drop-dead simple to use, Baker says. Apple has for now restricted the feature to Wi-Fi networks, meaning that if consumers love it, it'll give them one more reason to grumble about their service provider and generally increase Apple's leverage over the carriers.



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A 2009 Pinch Media study found that only 5% of those who download a free app are still using it 30 days later

Better Screen: Nothing steals the joy of owning an iPhone like a cracked touchscreen. Apple boasts that the iPhone 4's front and back glass casing is 13 times stronger than plastic, though analysts say it's only slightly sturdier than the stuff used for the past two generations of iPhones. Apple decided to talk about the glass strength to assuage concerns that the iPhone 4 is too fragile. To do that, they may still need to offer a plan that covers screen breakage.

HD

Software: The newly renamed operating system, iOS4, finally brings multitasking to the iPhone with the ability to organize apps into folders by category, such as sports. Better late than never, Jobs says. The real gems are iMovie editing software for high-def video and FaceTime, which will give Skype and Cisco Systems' Flip Video a run for their money. Single-use products continue to be vulnerable to Apple.

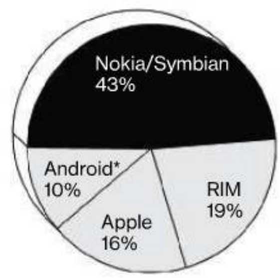






ACTUAL SIZE

0.37"



MARKET SHARE OF SMART PHONES Q1 2010, GLOBAL

*most of it from Motorola

verizon

(Not for now)

FRAME = ANTENNA

APPLE iPHONE SALES BY YEAR

2007: 3,704,000
2008: 13,675,000
2009: 25,105,000
2010 to date: 8,752,000

Gyroscope: Apple surprised the wireless industry with the addition of a three-axis gyroscope chip, the first phone to have one, says iSuppli analyst Jérémie Bouchaud. Paired with accelerometer chips already present, the iPhone 4 will be able to precisely detect tilting and rotating motions to power an impressive batch of new gaming features and navigation apps to help users find their way inside buildings, airports, and malls. It will be up to third-party app developers to make people care that the gyroscope is even there, but Apple has done very well relying on their ingenuity so far.

iAds: Apple has lined up an impressive list of advertisers willing to stake big bucks that they'll grab a lot of eyeballs on 100 million iOS4 devices worldwide. Apple manages the ad inventory and its important demographic data however, which might not sit well with big software developers who are looking for a larger cut of the mobile pie.

iBooks: Analysts accuse Jobs of using very rough math to back his claim that Apple has grabbed 22 percent of the U.S. eBooks market in just a few weeks. Still, 5 million books sold is impressive. Unless Amazon, Sony, and others quickly roll out color screens and offer readers the ability to sync reading across the iPad, iPhone, and iPod Touch, their days in the eReader business are numbered.

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Gatherings: Sovereign Debt Crisis

June 24th Barbican Centre, London

2010 Bloomberg Nations & Debt Briefing: Sovereign Debt Crisis is a gathering of the top public sector debt and finance ministers, institutional investors, and managers of sovereign wealth funds, private equity and hedge funds. Through the eyes of economists, bankers, ratings agencies and public sector debt managers, we'll look at the current state of, what's next for and investor reactions to the European financial malaise.

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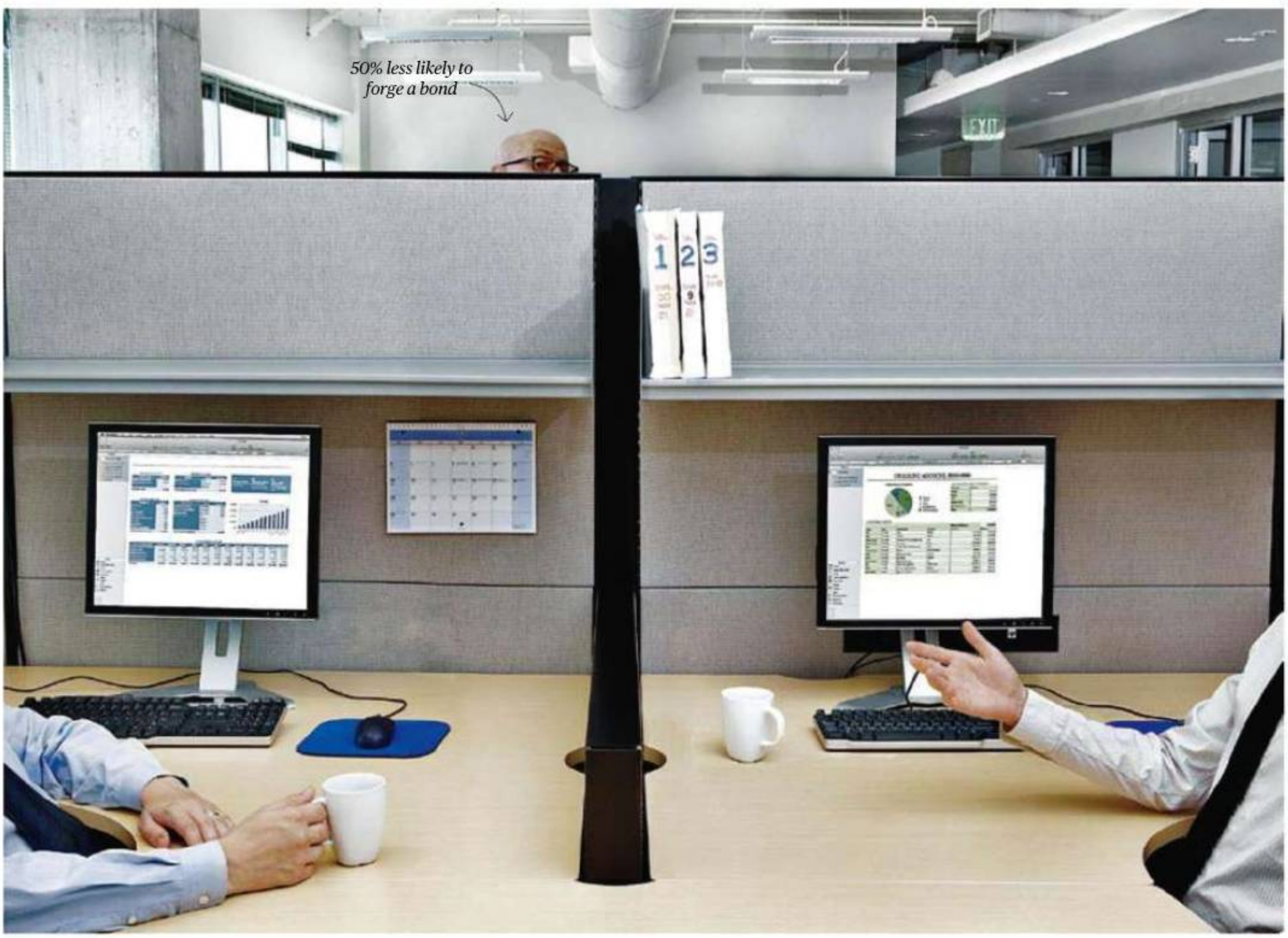
Microsoft
takes on Google
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Office 2010 & Junk Bonds & The Yankees

Etc.

How to
make the most
of London—and
still get to
Centre Court
Page 78





To the Vulnerable Go the Spoils

New evidence indicates that our ability to "click" with colleagues can make or break a career. *By Ori Brafman and Rom Brafman*

Photograph by Darren Braun

WILLIAMS: JULIAN FINNEY/GETTY IMAGES

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Etc. Social Studies

When she started her job as an accounting associate, Heather Moseley was assigned to a cubicle right outside the office of one of her organization's top supervisors, Kelly McVicker. Everyone in the office was curious about McVicker. She was poised, stylish, quietly intense, and very successful at her job. Her office seemed sequestered in a corner and, as Moseley soon noticed, the door was often shut.

One morning McVicker happened by Moseley's cubicle and noticed that she had a picture of Stevie Wonder as her screensaver. It was a seemingly insignificant observation, but it set in motion a series of life-changing events. As chance would have it, the previous week McVicker had seen Stevie Wonder at a restaurant, and she recounted to Moseley how he had swayed as he ate his curry. The two colleagues quickly hit it off, and when their conversation turned to Wonder's upcoming local show they immediately decided to buy tickets together. And so began a lasting professional and personal friendship.

Whether it's at a party or the office, we all know what it feels like to "click" with another person. Most of us, however, have not considered how it can impact more than our personal lives. New evidence suggests that clicking–and, in particular, a person's natural ability to click–plays a significant role in determining our career success.

By aggregating new research from various fields–since no specific discipline addresses the phenomenon– we endeavored upon a project to find what actually happens when two people click. More importantly, we wanted to discover if and how these moments shape our lives. While researching this topic, we initially discovered two big surprises. First, some people are more naturally inclined to form clicking relationships. Second, these people are *much* more likely to succeed in the workplace. Clicking at work can mean a promotion, a raise, or a position at the center of the company's social network. Take someone like Moseley. "I do an accountant's job, which is really administrative," she reflected. "Because of my relationship with Kelly, I now get invited to events, meetings, and conferences that I'd have no business going to as an accountant." Professionally, the relationship was mutually beneficial. "Knowing Heather," McVicker says, "I find out what's on people's minds. As a supervisor this is crucial information."

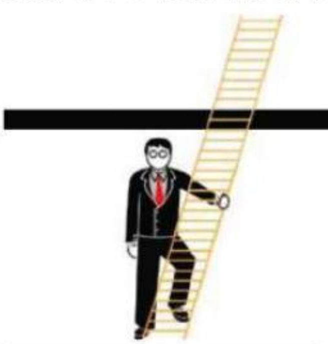
Being a high self-monitor comes naturally to some people. Think Bill Clinton or Oprah

Moseley wasn't strategically kissing up to a superior. Rather, she possesses a trait that University of Minnesota psychologist Mark Snyder has dubbed "high self-monitoring." By interviewing subjects about their ability to imitate the behavior of others and to become the center of attention, Snyder developed a scale of self-monitoring. High self-monitors, he discovered, are social chameleons. Without even realizing it, they adapt their personalities, behavior, and attitudes to fit the people around them. They pick up subtle social cues and tailor their responses to the situation.

Let's say you've been cornered at a party by someone who is talking your ear off about a topic you're indifferent to. Many of us would try to feign interest for a few minutes before excusing ourselves. A high self-monitor would find a way to make the discussion meaningful for both parties or segue naturally to another topic. In a lab experiment, for example, test subjects were placed next to a woman shaking her leg. Without thinking about it, high self-monitors were significantly more likely to shake their own legs, too.

At work this tendency translates to accelerated progression. When researchers at the University of Pennsylvania followed the careers of a set of business school graduates who were either natural clickers or not, they found the predefined high self-mon-

Self-Promotion



Employees who click are more likely to get promoted and be closer to the social nucleus of a company. Here are three quick ways to improve your odds of advancement.



1. Learn from natural-born clickers. Certain people, called high self-monitors, have an innate gift for forming instant connections. Emulate these lucky few by tuning in to others' emotional states and mirroring their energy levels.



2. Despite what you might think, vulnerability is a strength: The more we open up and share our feelings, the more trust we build and the more likely a connection becomes.



3. Your odds of clicking with someone rise significantly with every foot of proximity. Whether it's choosing a desk in the middle of the office or a seat near the middle of the conference table, the closer you physically are to people, the more likely you are to connect.

ILLUSTRATIONS BY JENNIFER DANIEL

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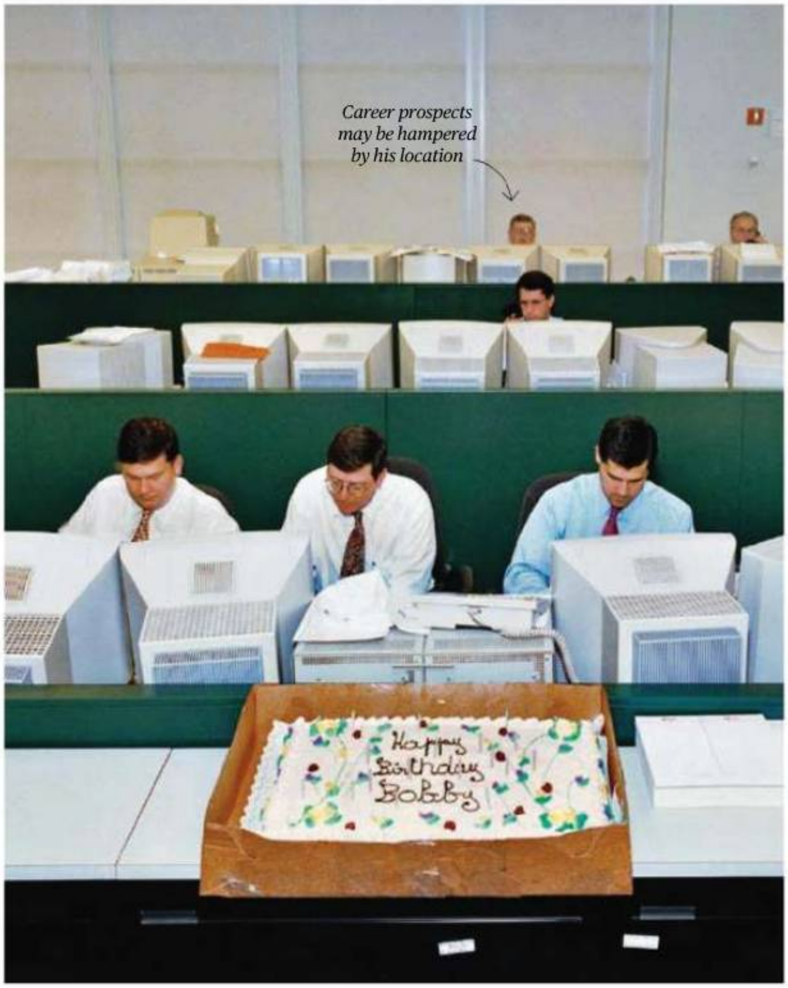
itors were significantly more likely to get promoted, both in-house and across different companies. A separate study of one particular high-tech firm with 116 employees, compiled by researchers at the University of Cincinnati, the University of Kentucky, and Pennsylvania State University, found that it took an average of just 18 months for high self-monitors to infiltrate the nucleus of their workplace network. For low self-monitors it took a staggering 13 years. "In a social situation, high self-monitors ask, 'Who does this situation want me to be, and how can I be that person?,' " says Snyder. "By contrast, low self-monitors ask, 'Who am I, and how can I be me in this situation?' "

Being a high self-monitor comes naturally to some people. Think Bill Clinton or Oprah Winfrey—people you'd want to have a beer with. Scientifically there is no way of knowing how much self-monitoring is innate vs. learned. (Psychologists believe it is a combination of both.) This means that even if high self-monitoring comes innately to some, we can all train ourselves to become higher self-monitors. While researching the topic we found several click accelerators. Two especially relevant to the workplace are proximity and vulnerability.

Is your office, for instance, in the middle of the action or off in a corner? McVicker's was at the end of the hall. While we might assume that she was a private person who selected an out-of-the-way office, what if the office placement itself was what made her appear somewhat aloof? Researchers studying college dorm residents discovered an odd pattern. Those living toward the center of the hall were far more popular than their counterparts at the ends. Regardless of where they lived, students were much more likely to hit it off with their next-door neighbor. Move one door down and the chances for a click went down by 50 percent. Move another door down and the chances went down by half again. The students at the ends of the halls simply had fewer close neighbors—and therefore suffered socially. Think of the person whose office or desk is right next to yours. You're twice as likely to form a bond with that coworker than with someone just a single office farther away. Your chances are halved again if you're separated by two offices. The more frequent our face-to-face interactions with a person, even without conversation, the more we tend to like him or her.

Researchers at the University of Pittsburgh reveal that encountering a stranger on 10 occasions instead of five makes us find that individual more attractive, intelligent, warm, and honest. By extension, showing up in person to a meeting rather than dialing in may be more important than we realize. The same goes for attending optional gatherings, keeping your office door open, and communicating in person rather than over the phone.

How much we reveal about ourselves—and our own vulnerability—also helps us click. One study conducted by SUNY-Stony Brook social psychologist Arthur Aron and his research team paired individuals who didn't know each other and assigned each a set of cocktail-party-type questions, such as "What did you do over the holidays?" The other half were given questions that required more intimate self-revelation, such as "What are your most treasured memories?" The pairs who were forced to be more vulnerable in their answers formed incredibly quick, deep connections. One pair even married.



Career prospects may be hampered by his location

LARS TUNBJORK/AGENCE VU/AURORA PHOTOS

It took some workers 13 years to get to the core of their office network. "Clickers" did it in 18 months

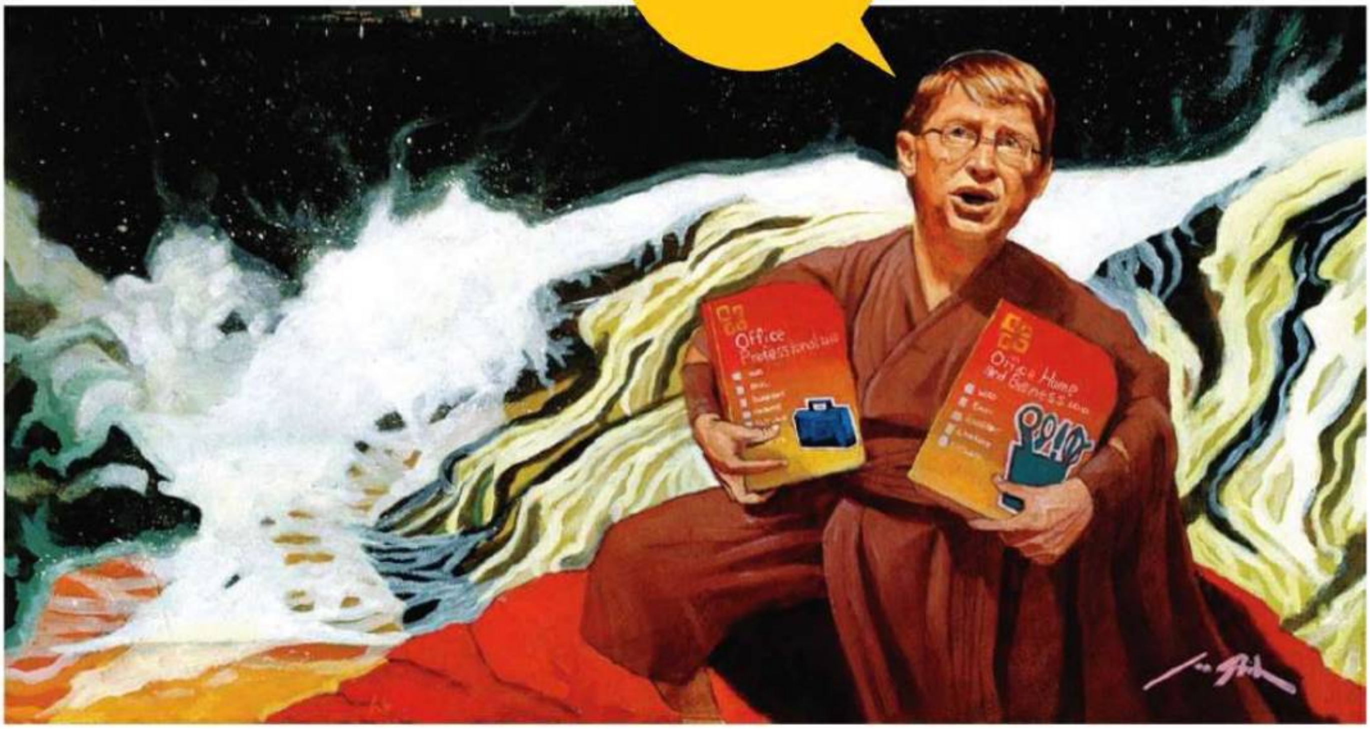
Our response to vulnerability is so innate that it can even be triggered by a machine. Harvard students who were asked by a computer to answer intimate questions—such as "What have you done in your life that you feel most guilty about?"—were understandably reluctant to share. Yet when the computer "self-disclosed," prefacing its questions with a "confession" such as "There are times when this computer crashes for reasons that are not apparent to its user," students were significantly more forthcoming. It turns out that when we disclose our feelings, we send a message of trust to others, making it easier for them to relate to us more openly.

Office managers, take note: The presence of high self-monitors can be contagious. Reflects McVicker, "I became more invested in the culture, more emotionally attached to my colleagues." B

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Etc. Hands On

Microsoft Office 2010 embodies Bill Gates' philosophy of "embrace and extend"



Microsoft Heads Into the Cloud

Office 2010 offers a lot, but beating Google is another matter. *By Rich Jaroslovsky*

Microsoft is finally getting the hang of this software thing. After years of problematic products that tarnished its reputation and at a time when its model of prepackaged, locally installed software is under unprecedented assault from Web-based alternatives, the company is showing signs it can respond to the mortal threats it faces.

First came last fall's Windows 7–the clean, stable successor to the unlamented Vista operating system–which finally gave businesses and consumers a compelling reason to upgrade their existing setups. Now comes a new version of the company's other great cash cow, Microsoft Office, which improves the world's most widely used productivity software.

More is at stake, however, than just profits. Microsoft, beset by stumbles in such critical areas as mobile phones, is under pressure to prove its relevance in a changing marketplace. Office does so by preserving its traditional approach while acknowledging that computing in the cloud–distant online servers–isn't just a fad. It's the old Bill Gates philosophy of "embrace and extend" brought up to date.

Office 2010, which goes on sale June 15, isn't the wholesale overhaul that its predecessor, Office 2007, represented. This is refinement, not revolution: The file formats remain the same, and most users who are content with what they can accomplish using their current version will have little reason to spring for the upgrade. At the same time, the new version adds scads of features to the suite's core applications–Word, Excel, PowerPoint, and Outlook–without burying usability in the process. It also scales back a few of Office 2007's excesses and, perhaps more significantly, braces Microsoft for the coming battle with archenemy Google that will play out across a number of fronts in the next several months. Netbooks running Google's Web-centric Chrome operating system may show up later this year. Meanwhile, Microsoft continues to pour resources into Bing, the latest effort to dent Google's supremacy in search. Nowhere, however, is the war likely to be hotter than in productivity software.

Google's weapon of choice, its online suite of programs called Google Docs, is more than just competition: It's an assault on Microsoft's entire being. Google

i

Office 2010

Professional version ($499) includes publishing and database applications in addition to Word, Excel, and PowerPoint



ILLUSTRATION BY JON STICH

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Docs is software as a service; both the programs themselves and your data reside in the cloud, to be summoned as needed from any Internet-connected computer and dismissed when you close your browser. And, in its simplest form, Google Docs is free.

Microsoft Office decidedly isn't free. The basic consumer version, called Home and Student, will cost $149; it includes Word, Excel, and PowerPoint but lacks Outlook, Microsoft's e-mail and calendar client. The Home and Business edition, which includes Outlook, will list for $279; Office Professional, which also includes publishing and database applications, will go for $499.

The big news about Office isn't what's in the shrink-wrapped package, though. It's what's on the Web. For the first time, Microsoft is offering Internet-based versions of Word, Excel, and PowerPoint. These apps, like Google's, are free, but unlike Google's, they aren't intended for use in lieu of Office programs installed on your hard disk. While they can be used purchasing Office 2010, Microsoft has crafted them more as adjuncts to the programs you've paid for, facilitating online collaboration and mobile access to your work.

The 2007 version of Office marked a radical revamp of the software. Gone was the familiar structure of pull-down menus through which you reached ever-more-arcane functions and features. In its place, Office 2007 introduced what Microsoft calls "the ribbon"–customizable strips of controls that sit atop your spreadsheet or memo, changing when you click a tab corresponding with the general task you want to accomplish.

Office 2010 keeps the concept of the ribbon, which should make the learning curve considerably easier. It even extends it, most notably to Outlook, which also gains new ways to organize e-mail threads into conversations and the ability to function with such social networking sites as Facebook and LinkedIn.

The new Office also incorporates some welcome changes. For instance, File is back. In Office 2007, that venerable item was replaced in the upper-left corner of the navigation with a shiny Office logo. It wasn't readily apparent that you had to click the logo to access the old File options. (You know, those unimportant commands like New, Open, Save, and Print.) In Office 2010, File has been resurrected as a tab that takes you to a new area Microsoft calls Backstage. Here the traditional commands coexist with options to set permissions on who can do what to your document, check to make sure it is compatible with older versions, and share it via e-mail, the Web, or a server on your company's network.

Heavy users of the ubiquitous PowerPoint presentation software are likely to gain the most from the new Office. Microsoft has significantly expanded the picture-editing tools, making it less likely you'll have to duck over to Adobe PhotoShop mid-project to get those graphic effects just so. There is also the ability to embed and tweak videos in PowerPoint slides, and add-ons available on the Web can broadcast a presentation over the Internet to viewers who don't have the software installed on their computers.

The Excel spreadsheet, meanwhile, has introduced something called Sparklines, minicharts that reside within a cell and render small bits of data graphically. Word even lets you recover unsaved versions of your documents. Besides allowing you to save your work to your local hard drive, Office 2010 allows anyone with a Hotmail account or other Microsoft-issued ID to make use of SkyDrive, 25 gigabytes of free online storage. Once your work is stored on the cloud, you–or whomever you designate–can access it using the new Office online apps.

These online versions of Word, Excel, and PowerPoint are designed to evoke their locally installed counterparts without precisely duplicating them. They too make use of the ribbon interface, and if they lack the full scope and power of the paid Office programs, they provide more than enough functionality for most users.

The big question for Microsoft–and Google–is how users will want to utilize productivity software. If the world remains PC-centric, Office 2010 will be a winner. If the cloud eventually supplants the desktop, the new Office Web Apps will keep Microsoft in the game, but that game will be a lot less profitable. B

The latest edition of Word lets you recover unsaved versions of your documents

R.I.P. Clippy



ILLUSTRATION BY QUICKHONEY

Last summer, Microsoft produced a trailer for a faux action thriller, *Office 2010: The Movie*. The viral campaign, which became a YouTube hit, was designed to promote the latest suite of desktop applications. The film is best-remembered by some for reviving Clippy, the animated paperclip-shaped Microsoft "Office Assistant." About halfway through, a close-up on Clippy's tombstone puts to rest any hopes of a comeback. It's inscribed with the years of his short digital life: 1997-2004.

To savvy Microsoft users, Clippy's grave site evokes memories of other goofy, defunct Office Assistants, the first of which–a yellow dog named Rover–was meant to help users navigate the 1995 software product Microsoft Bob. With the release of Office 97 came others such as Kairu the Dolphin, PowerPup the Dog, The Genius (a caricature of Albert Einstein), Will (a cartoon of Shakespeare), and Bosgrove (a butler).

Many users found them irritating, Clippy especially. "He was a little presumptuous, a little annoying," says Kevan Atteberry, the designer who created him. "People thought, 'I know how to do it. I don't need your help.' "

The 2010 version doesn't include any animated assistants. The dog, the robot, the shape-shifting dot: These characters are long gone. And so, too, is that pesky paperclip.
—*Spencer Bailey*

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Invest in ↓



Embracing Risk–And Blue Chips

Morgan Stanley strategist David Darst eyes U.S. "superstars," Europe, and junk bonds

Many of our strategists think the market will be largely range-bound and move sideways as it did from 1966 to 1982, when it gained only 15 percent. We see the recent volatility as a correction, not the beginning of another downturn. The stock market is in pause mode midway through a two-to-three-year bull market in risk assets–meaning junk bonds, corporate credit, real estate investment trusts (REITs), commodities, emerging-market stocks, Canada, and Australia. We are overweight risk asset classes and underweight cash, Treasury inflation-protected securities, and U.S. government securities. This was a brilliant call until the market selloff.

We're aware of the headwinds in the U.S., such as home prices and joblessness. There's also China as it tightens monetary policy and the European sovereign debt crisis. U.S. taxes will go up at the end of the year if no one does anything, and that's another headwind. Completing financial services legislation, according to Barney Frank, will take the month of June. These unresolved things have the potential to rattle the market.

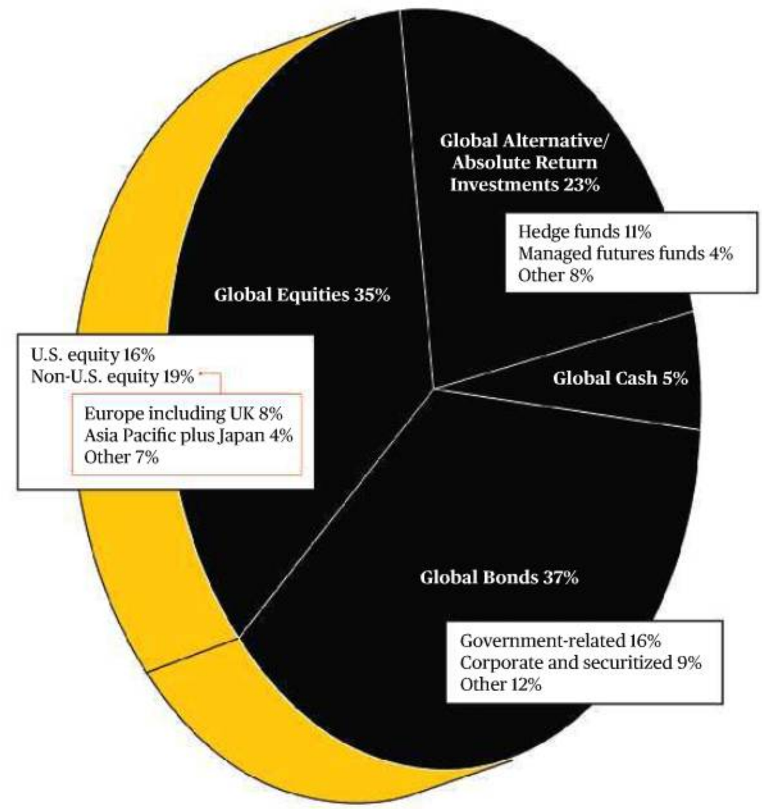
At the same time, though, there's growth in corporate profits in the U.S., Europe, Japan, and emerging markets. Interest rates and inflation are low. Monetary policy is still stimulative, although there is some tightening around the world. In the U.S. there is good corporate liquidity, and we're seeing mergers and acquisitions, dividend increases, and stock buybacks.

Investors need to recognize they have superstar companies sitting here in the U.S. Just look around you: Giants like IBM, Johnson & Johnson, Procter & Gamble, Medtronics, and Schlumberger are selling at the same price multiples as small-cap and mid-cap stocks.

Outside of the blue chip universe, we like junk bonds. In the latest market selloff, the spread between average junk bond yields and Treasuries opened up by 150 basis points. [A basis point is one one-hundredth of a percent.] Junk bonds are attractive because spreads are wider–you're getting paid more for taking some risk–and the economy is improving. It's tough for a small investor to get a good price buying individual junk bonds, so they should invest through an exchange-traded fund, a closed-end fund, or an open-end mutual fund. For instance, there's the SPDR Barclays Capital High Yield Bond ETF.

HOW MORGAN STANLEY GLOBAL SLICES THE PIE

Recommended asset allocation for a long-term U.S. investor with a global focus



DATA: MORGAN STANLEY SMITH BARNEY GLOBAL WEALTH MANAGEMENT GROUP; AS OF MAY 2010

We expect [European] earnings to go up 59 percent over the next 12 months

We like U.S. stocks, but our European strategist went overweight in European stocks on May 21. Europe is so cheap, selling at 11 times earnings. We expect earnings on the MSCI Europe Index to go up 59 percent over the next 12 months. In Europe, we're focusing on pharma, energy, and materials. We like companies like Roche, Glaxo SmithKline, AstraZeneca and Total, the French energy company. In Canada, we like companies like Toronto-Dominion Bank, Suncor Energy, and Canadian Natural Resources. B

—*As told to Christopher Farrell*

The Stats: David Darst is managing director and chief investment strategist of Morgan Stanley Smith Barney Global Wealth Management Group. He is the author of *The Little Book that Saves Your Assets* (Wiley).

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Etc. One True Thing

The Desk Lamp

Brighten your workplace without cramping your style

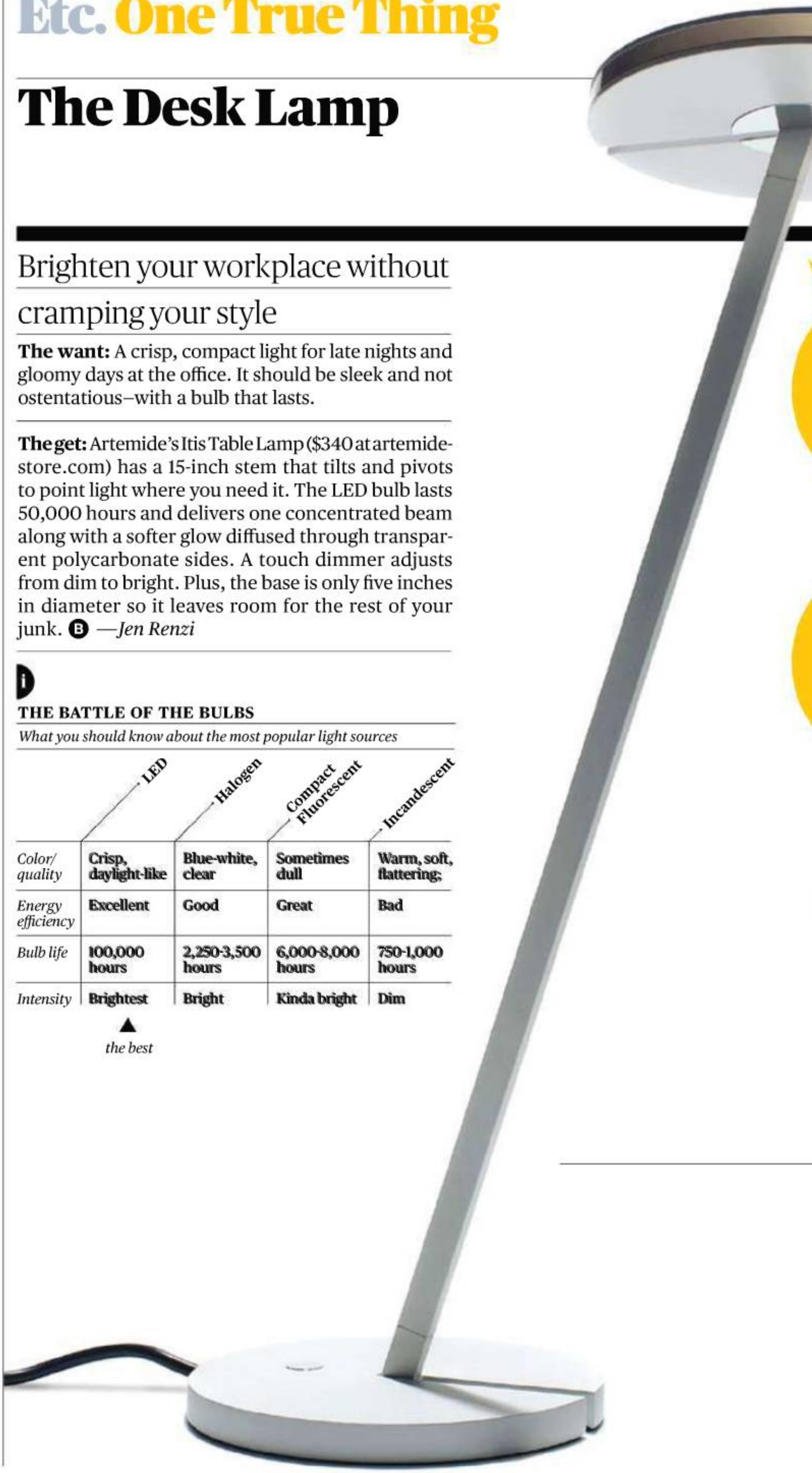
The want: A crisp, compact light for late nights and gloomy days at the office. It should be sleek and not ostentatious—with a bulb that lasts.

The get: Artemide's Itis Table Lamp ($340 at artemide-store.com) has a 15-inch stem that tilts and pivots to point light where you need it. The LED bulb lasts 50,000 hours and delivers one concentrated beam along with a softer glow diffused through transparent polycarbonate sides. A touch dimmer adjusts from dim to bright. Plus, the base is only five inches in diameter so it leaves room for the rest of your junk. B —*Jen Renzi*

THE BATTLE OF THE BULBS

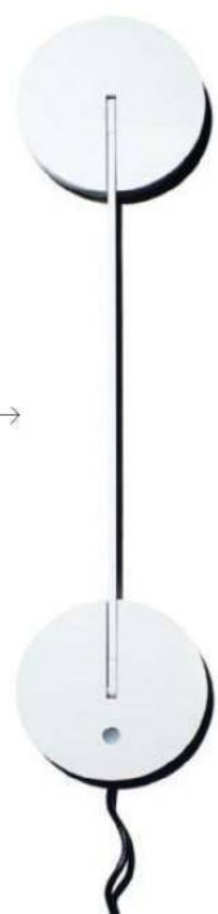
What you should know about the most popular light sources

	LED	Halogen	Compact Fluorescent	Incandescent
Color/ quality	Crisp, daylight-like	Blue-white, clear	Sometimes dull	Warm, soft, flattering;
Energy efficiency	Excellent	Good	Great	Bad
Bulb life	100,000 hours	2,250-3,500 hours	6,000-8,000 hours	750-1,000 hours
Intensity	Brightest ▲ *the best*	Bright	Kinda bright	Dim



The steel head rotates 180 degrees to cast light on your desk, up to the ceiling, or on the walls

It takes 10 seconds to fold the lamp flat so you can pack it away when you need extra room



PHOTOGRAPHS BY JAMIE CHUNG FOR BLOOMBERG BUSINESSWEEK

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Wimbledon

A personalized guide to London's swanky shops, hippest bars—and the world's most genteel



The Wimbledon Lawn Tennis Museum



The courtyard at the Sanderson Hotel

1. The Tennis Freak

For those eager to camp out overnight for day-of tickets and who will stay in their seats through wind, rain, and rare spates of blistering sunshine: Here is where to watch, celebrate, mourn, and step up your own tennis supplies.



Sleep: The new **H10 Hotel** has a handy Waterloo location (the tube to Wimbledon takes 20 minutes), a $240 per-night rate, and a contemporary look. **Eat:** If you can drag yourself away from the grass, **Bluebird** in Chelsea serves Cornish mackerel and nettle risotto and shows matches on a big screen. **Shop:** The West End's **Wigmore Sports** restrings rackets and sells wild neon tennis attire that would outrage Wimbledon's buttoned-up referees (players are required to wear white). **Drink: The Dog & Fox** in Wimbledon Village is where players drown their sorrows when they're booted by a better opponent from the banana-and-Gatorade path. **See:** What better than to putter around the **Wimbledon Lawn Tennis Museum**? Delights include a recreation of the 1980s men's dressing room and Rafael Nadal's pirate-length trousers. **Wimbledon Tip:** Prove your devotion by camping out in the (cash-only) ticket queue, or score a Centre Court seat by watching ticketmaster.co.uk with hawkeye diligence. Prices start at $37, and you can sign up at wimbledon.org to get an e-mail when they go on sale.



2. The Corporate Executive

Fueled by strawberries and tea instead of curry and ale, discerning Britons have brought clients to Wimbledon since the first championship was played in 1877. Follow their lead, then wine and dine at these choice summer spots.



Sleep: Get St. James luxury at the recently revamped **Dukes Hotel**, which has a courtyard cigar bar and rooms looking onto Green Park. If you can swing it, book the 700-square-foot penthouse for its balcony and glorious views. **Eat: The Wolseley** is a Mitteleuropean bastion—the menu ranges from schnitzel to perfectly crisp crème brûlée—and a stomping ground of the city's elite. **Shop:** The famed grocery store **Fortnum & Mason** peddles fancy teas, cheeses, and addictive house-brand fudge. **Drink: The Sanderson Hotel**'s courtyard has all the elements of the perfect summer refuge: pools of reflected water, fragrant overgrown flowers, and cocktails made with fresh ginger, cucumbers, and figs. **See:** The Summer Exhibition at **The Royal Academy of Arts**, where amateur artists' work hangs next to paintings by established British stars. It runs June 14-Aug. 22. **Wimbledon Tip:** For $1,500 a day, the **Gatsby Club** smoothes your way onto Centre Court by way of champagne bars, three-course meals, afternoon tea, and shuttles from Southfields station.



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Spanish star Rafael Nadal will try for his first Wimbledon title



sporting event



The bar at Town Hall Hotel in London's East End



Kensington's Diana Memorial Playground

3. The Twenty-Something



Join the hipsters and beatnik Brits who hang around new restaurants, bars, and hotels in London's edgy Shoreditch and Clerkenwell neighborhoods. Score a last-minute ticket for cheap or watch with the rowdies at a cool local pub.

Sleep: Town Hall Hotel just opened in rapidly gentrifying Bethnal Green. Its chef trained at Spain's renowned El Bulli, and ultramodern rooms are $250 a night. **Eat:** Brave **Polpo's** net curtains and you'll find a wildly popular Venetian-style bacaro dishing up small plates like pork belly with hazelnuts and radicchio or pizzetta bianca. They don't take reservations, but you can wait for a table in one of many bars nearby. **Shop:** Get to Shoreditch's Redchurch Street to buy reinventions of classic, logo-free '60s polos and T-shirts from the new **Sunspel** shop. **Drink:** The area around Exmouth Market mixes alfresco drinking with moderate urban grit. Its **Café Kick** celebrates soccer before tennis (with vintage foosball tables to prove it) but still shows Wimbledon–and pours the city's finest mojitos. **See:** Find bargains and fresh ideas at **Free Range**, a show of young fashion designers running June 4-July 22. **Wimbledon Tip:** When corporate types leave by teatime, their courtside tickets are resold; fair-weather fans can buy them for $8 and see some choice sundowner tennis.



4. The Family



London is not known as an affordable family destination, but the dollar is worth 25 percent more against the British pound than it was in 2008. Bring the kids and make an example of how the Williams sisters settle sibling rivalry.

Sleep: A Place Like Home rents apartments near parks in tony South Kensington. Two-bedroom walkups start at $750 a week. **Uniquely a Place Like Home**, its sister site, offers fancier two-bedrooms on leafy squares for around $2,600 a week. **Eat:** The Tuscan fare at **La Famiglia** goes over well with picky young eaters–and it tastes ambrosial to adults. **Shop:** In the business of turning children into consumers since 1881, **Hamleys** toy store sells four-tube packs of self-descriptive Magic Plastic that cost $15 and keep kids entertained for hours. **Drink:** In chic Bayswater, down oysters and swill prosecco at the plush **Commander Bar**, which features in-house day care and free sitters on weekend afternoons. **See:** Head across the street to Kensington Gardens' fantastical pirate-ship playground, named after Diana, Princess of Wales. **Wimbledon Tip:** The week before the tournament, watch qualifying rounds–for free–at **The Bank of England's Sports Centre** in Roehampton, six miles south of Central London. —*Sarah Turner*



ILLUSTRATIONS BY KAGAN MCLEOD; NADAL: BERTRAND GUAY/AFP/GETTY IMAGES; PARK: KEN GOFF/TIME LIFE PICTURES/GETTY IMAGES

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“I’m always hardest on the biggest guy on the team,” Steinbrenner said. “I’m a football guy”



The Madness—and Method—of King George

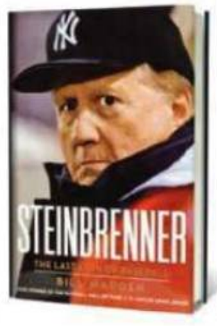
Bluster was a crucial part of George Steinbrenner’s theory of managing. *By Jesse Kornbluth*

In his 80th year, George Steinbrenner is said to have mellowed dramatically. This unlikely transformation is not the result of a late-life personal reckoning. According to sources, it’s the by-product of a series of attacks that have temporarily reduced the flow of blood to his brain, leaving confusion and dementia in their wake. Whatever the cause of Steinbrenner’s decline, there is no doubt that the biggest bully in the history of professional baseball no longer leaves his employees trembling.

As Steinbrenner moves closer to that place where World Series rings don’t matter, it does no one—well, no one outside of the Steinbrenner clan—any good to speak nostalgically about the New York Yankees’ majority owner as a “lion in winter,” as many have. Not, that is, when impressionable readers of *Steinbrenner: The Last Lion of Baseball* can take the wrong lesson from his financial success. Because the math is indeed sensational: In 1973, Steinbrenner contributed just $168,000 of his own money to a group of investors who bought the team for less than $10 million; in 2009, *Forbes* estimated the Yankees’ value at $1.5 billion and the Steinbrenner family’s assets from baseball—stemming mainly from its hagiographic YES Network and share of a concessions company—at $2 billion to $3 billion. Given that level of asset appreciation, some entrepreneur might sensibly conclude that Steinbrenner had a rare gift for business and try to imitate his methods.

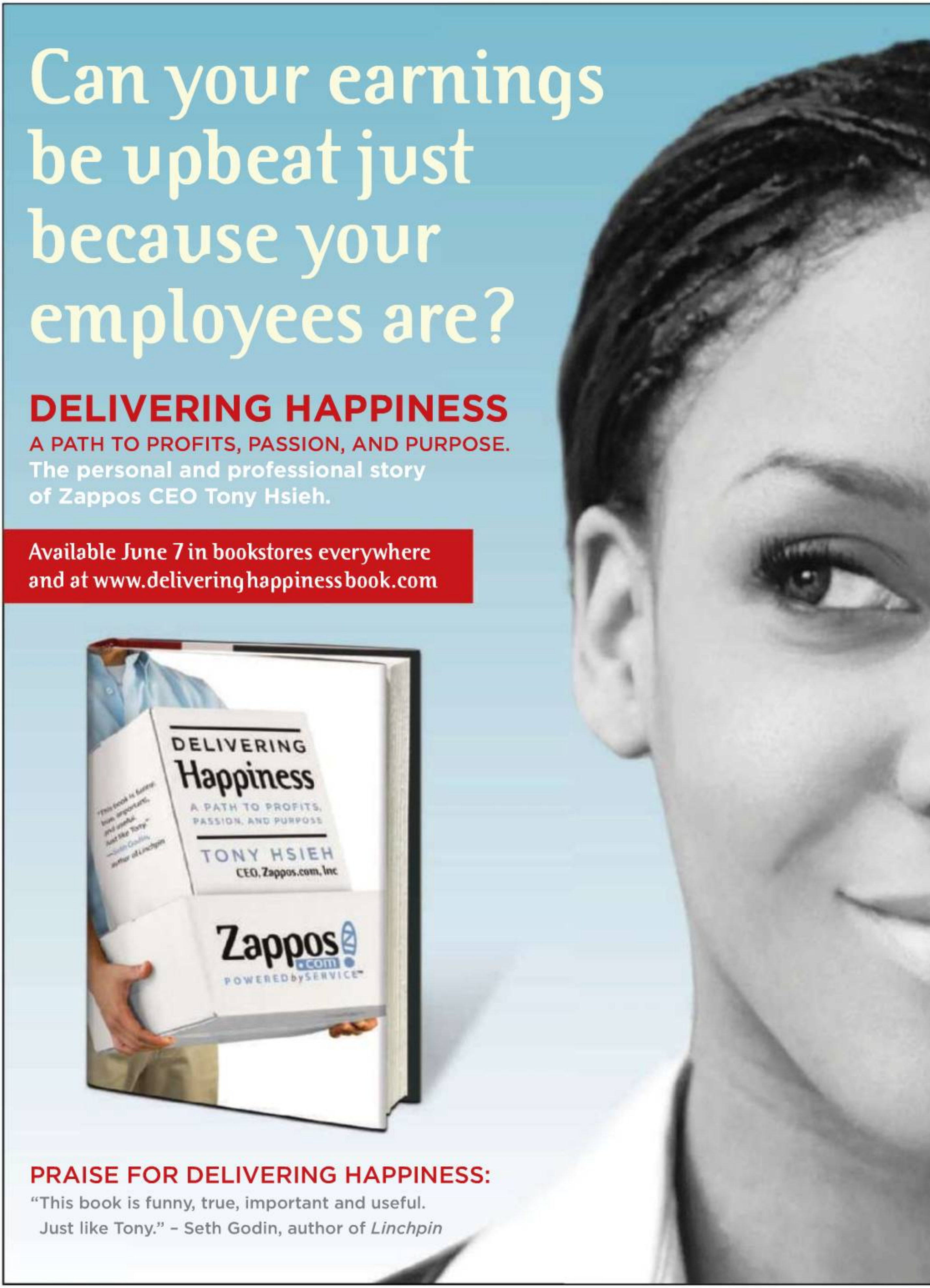
By the numbers, there’s no argument that Steinbrenner produced a dynasty. His Yankees have won seven World Series titles. Some of the greatest stars of his era wore pinstripes: Reggie Jackson, Dave Winfield, Catfish Hunter, Thurman Munson, Bernie Williams, Derek Jeter, Alex Rodriguez, Mariano Rivera—and that’s just a quick pass at a Yankees highlight reel. Clearly, the principal owner had something to do with his team’s dominance during the long decades of his rule. But what exactly was his contribution? Was it just his checkbook? Do his “baseball people” and his managers deserve some, or most, of the credit? Could his teams have been as successful without his incessant second-guessing, compulsive harassment, and gratuitous

Steinbrenner: The Last Lion of Baseball
By Bill Madden
HARPER; 480 pp, $26.99



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Etc. The Stack

cruelty? And here's the essay question for business school ethics courses: Were his teams' triumphs worth the price he made others pay?

For all his erratic behavior, Steinbrenner did have a management theory: "I'm always hardest on the biggest guy on the team. I feel that's the way to motivate the other players. I'm a football guy, and that's how the great coaches in football do it." He applied this approach to Jackson, Winfield, Don Mattingly, and Goose Gossage—with predictable results. "You come here, you play, you get money, and that's it," Mattingly fumed. "They think that's respect."

Bill Madden, who covered the Yankees for the New York *Daily News* for more than three decades and conducted more than 150 interviews for this book, says he still can't decide if Steinbrenner should be in the Hall of Fame. He prefers instead to "faithfully tell his story." Not exactly the boldest point of view, but the story does speak for itself, and the Hall of Fame is the least of it—this is the biography of an unloved boy who grew up to be an unlovable executive.

As Madden outlines Steinbrenner's childhood, it's postcard simple. Nothing George Steinbrenner ever did was good enough for his father, and, later, George's surrogate children never satisfied him. He kept everyone in his organization off-balance, hiring and firing and rehiring in a blizzard of unfocused rage. In 1982 he burned through three managers, five pitching coaches, three hitting instructors, and 47 players. All to end the season in fifth place.

His style was even less effective with his off-field employees. Horror stories abound: firing a $50,000-a-year public-relations man three days before Christmas; reaming an aide who called "heads" in a coin toss that would determine the home stadium for a playoff game because, he screamed, "Don't you know tails comes up 70 percent of the time?" (It came up tails.)

After winning the World Series in 2000, Steinbrenner deprived coaches of bonuses and scouts of rings. He decided to eliminate dental benefits, forced executives to scrape gum off stadium ramps, and even criticized the inspiring one-handed pitcher, Jim Abbott, for his charity work. Most memorably, he turned Billy Martin into a human bungee cord. (Has any chief executive in any business ever hired and forced out one guy five times?)

Like Donald Trump, Steinbrenner had the great good fortune to be a larger-than-life character at a time when increased media exposure fed America's obsession with celebrity. As a result, many of his defects became assets. By paying outrageous salaries and launching blood feuds with his own employees, Steinbrenner made headlines for himself and money for the media. In return, the media made money for him.

He may have been a bumbler, a meddler, an out-of-control Machiavelli, but when it came to making broadcasting deals, selling corporate boxes, and securing public funding for a new stadium, Steinbrenner was the guy sitting under the TV lights—and dictating terms. He deserves credit for grasping the power of cable TV and for understanding how signing foreign players would transform his team into an international brand and stretch the Yankee banner across the planet. He was convinced that his outsize belief in the importance of the Yankees would convince others of the same.

Readers of Michael Lewis' *Moneyball* know there's another way to run a baseball team effectively. As Lewis describes the management theories of Billy Beane, the general manager and minority owner of the Oakland Athletics, a deep relationship to statistics about baseball players may be more valuable than an open checkbook. Yet speed, taking pitches, and consistency were of no interest to Steinbrenner—he didn't want to play "small ball" if he could afford to stock his roster with home-run hitters.

Steinbrenner ignored innovation. He went by his gut and had no use for common sense. To funnel money to Richard Nixon's reelection campaign, he chose to break the law rather than write a larger check himself. To humiliate Dave Winfield, he accused the Yankee slugger of loaning money at outrageous interest to a man Steinbrenner knew was a gambler. Even Derek Jeter—the first Yankee since Lou Gehrig to be beatified while still wearing pinstripes—got knocked, in 2002, for using the off-season to enjoy his bachelor status.

The elegance and beauty of baseball were not what drew Steinbrenner to the game; for him, it was merely a convenient arena in which he could wage war and test the limits of his power. As he looked at life, he was Mr. Big, everyone was out to get him, and so he had to get them first. When he gave Jeter a book, it was *Patton on Leadership: Strategic Lessons for Corporate Warfare*. To Bill Madden, he recommended the teachings of Attila the Hun.

There's no evidence that he benefited from these books. What's most remarkable about Steinbrenner as an executive is his seeming incapacity to learn from experience. Banned from baseball for more than two years, he celebrated his return by posing as Napoleon for the cover of *Sports Illustrated*. Over and over in these pages he claims all the oxygen in the room for himself. As one of his investors noted: "There is nothing in life quite so limited as being a limited partner of George Steinbrenner." Ⓑ

You're Fired!

Long before another voluble executive made waves for dismissing (and alienating) employees, George Steinbrenner ran a tight ship—with positive and negative results:



Billy Martin

The legendary manager led the Yankees on five occasions during the '70s and-'80s. He was fired or forced out each time.



Dave Winfield

Though he signed the slugger to the game's richest salary in 1980 (10 years, $23 million), Steinbrenner so despised his star that he paid a source to unearth embarrassing details about the player.



Buck Showalter

Despite leading the Yankees to their first postseason apparance in more than a decade, Steinbrenner fired Showalter after losing to the Mariners in the 1995 Division Series. His replacement, Joe Torre, went on to win four championships.

FROM TOP: FOCUS ON SPORT/GETTY IMAGES (2); AP PHOTO

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Etc. Hard Choices

Robert Nardelli

"I had no choice but to cut staff.... I had to lay off 5,000 salaried people the Wednesday before Thanksgiving"

The former CEO of Chrysler on cutting 35,000 jobs in order to save his company during the financial crisis



I signed on as Chrysler CEO in July 2007. The industry was robust, but the brand had lost its identity. The first six months were great. We rebuilt the brand, disentangled it from Daimler, pruned the product line. Then came the financial crisis. The first thing we lost was leasing; 20 percent of our business disappeared overnight. Then the fleet business went away, and financing for new car purchases dried up.

It soon became clear that we were in a battle to survive. We cut $5 billion in costs and brought the capacity down by 1.4 million units. It wasn't enough.

The toughest decision I had to make was reducing the workforce by 35,000 people. We desperately needed to preserve cash to keep the supply chain intact. We could have sold assets or furloughed union employees, but because of contractual obligations neither of those options would have made us cash-positive.

I had no choice but to cut staff. It was traumatic releasing them into an economy where it wouldn't be easy to find another job. I had to lay off 5,000 salaried people the Wednesday before Thanksgiving. I remember going into a large staff meeting and seeing that the crowd in the auditorium was half what it had been when I started as CEO. It was such a haunting visual.

The union was on board. We all recognized that we were one step away from cataclysm. The UAW didn't roll over, but it recognized that we were in it together. If we hadn't made layoffs, we would not have gotten the first $4 billion from the government. Every supplier would have felt the domino effect.

The 10 percent unemployment rate is misleading. The real figure is closer to 18 percent. Unless this country creates 150,000 new jobs every month for the next four years, we won't get back to where we were in 2007. We need specific programs built to create new jobs–real jobs, not census jobs, not seasonal jobs.

As gut-wrenching as my decision was, it was critical to saving the company. A lot of families made big sacrifices for Chrysler, and I will never forget that. B

—As told to Diane Brady

PHOTOGRAPH BY MIKE MCGREGOR FOR BLOOMBERG BUSINESSWEEK

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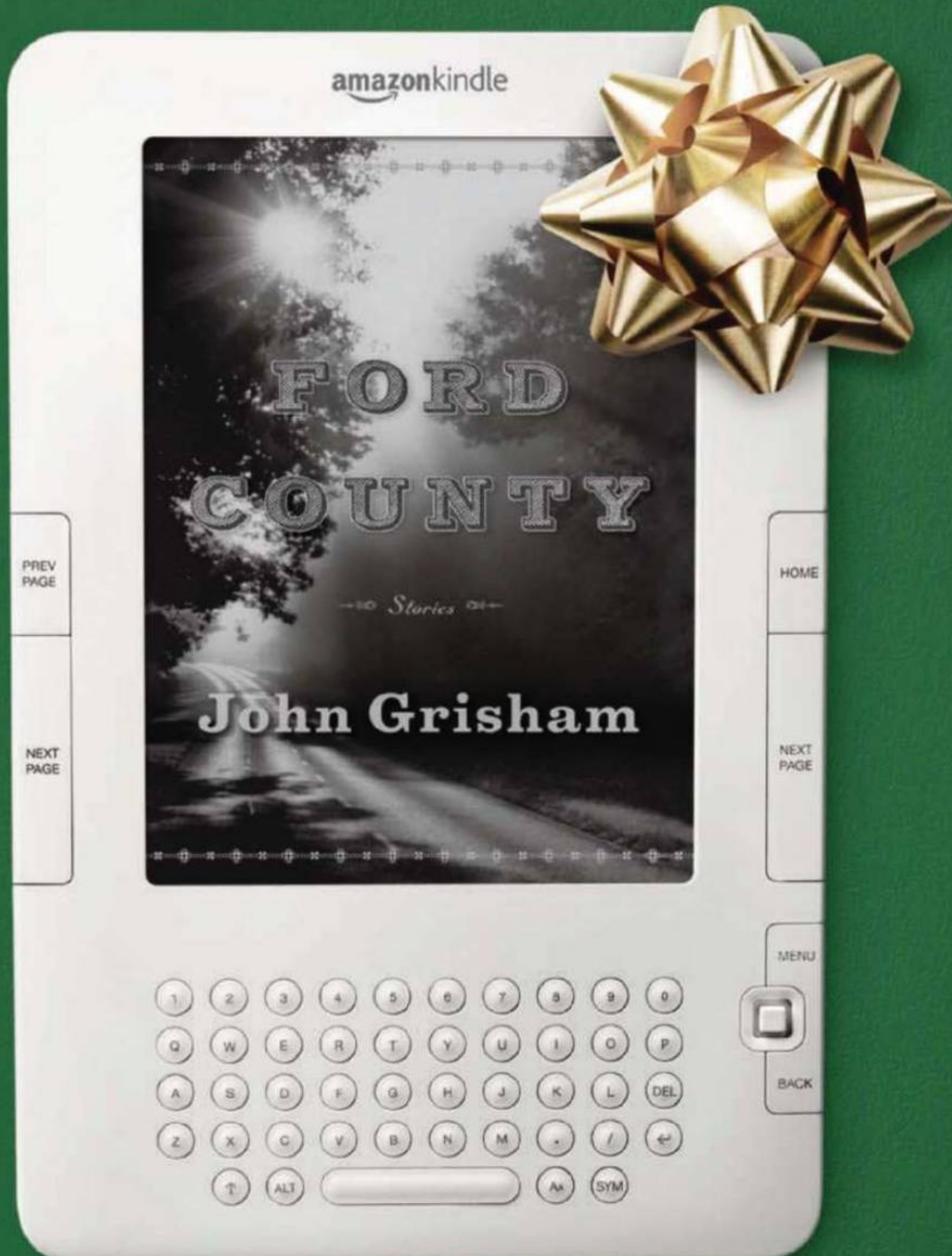
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